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OKTA.OQ - Q2 2020 Okta Inc Earnings Call

EVENT DATE/TIME: AUGUST 28, 2019 / 9:00PM GMT

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PRESENTATION

Operator

Good day, and welcome to the Okta Second Quarter Fiscal '20 Earnings Call. Today's conference is being recorded. At this time, I would like to turn the conference over to Dave Gennarelli. Please go ahead.

Dave Gennarelli - *Okta, Inc. - IR Executive*

Good afternoon, and thank you for joining us for today's conference call to discuss the financial results of Okta's second quarter of fiscal 2020. With me on today's call are Todd McKinnon, Okta's Co-Founder and Chief Executive Officer; Bill Losch, the company's Chief Financial Officer; and Frederic Kerrest, the company's Co-Founder and Chief Operating Officer.

Today's call will include forward-looking statements pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995, including but not limited to statements regarding our financial outlook and market position. Forward-looking statements involve known and unknown risks and uncertainties that may cause our actual results, performance or achievements to be materially different from those expressed or implied by the forward-looking statements. Forward-looking statements represent our management's beliefs and assumptions only as of the date made. Information on factors that could affect the company's financial results is included in its filings with the SEC from time to time, including the section titled Risk Factors in its previously filed Form 10-Q.

In addition, during today's call, we will discuss non-GAAP financial measures. These non-GAAP financial measures are in addition to and not a substitute for or superior to measures of financial performance prepared in accordance with GAAP. Reconciliation between GAAP and non-GAAP financial measures and discussions of the limitations of using non-GAAP measures versus their closest GAAP equivalents is available on our earnings release. You can also find more detailed information in our supplemental financial materials, which include trended financial statements and key metrics posted on our Investor Relations website.

On today's call, we will quote a number of numeric or growth changes as we discuss our financial performance. And unless otherwise noted, each such reference represents a year-on-year comparison.

And now I'd like to turn the call over to Todd McKinnon. Todd?

Todd McKinnon - *Okta, Inc. - Co-Founder, Chairman & CEO*

Thanks, Dave, and thanks, everyone, for joining us today. Our results mark another exceptional quarter of execution and financial performance. Total revenue grew 49%. Subscription revenue grew 51%. Calculated billings grew 42%. And remaining performance obligations, or RPO, grew 68%. We added 450 new customers in the quarter, bringing our total customer count to 7,000. Once again, we made broad additions across our enterprise customer base with 46% growth in customers with annual contract value greater than $100,000. And once again, over half of these additions were from new customers. We now have over 1,200 of these $100,000-plus customers, which demonstrates our enterprise momentum and the increasingly strategic role that Okta plays in our customers' environments.

Our momentum is powered by the massive and inevitable shifts that are enveloping companies today. The rapid growth of cloud and hybrid IT, digital transformation and security. Identity plays a critical role in each of these megatrends, and organizations are turning to Okta because we are uniquely able to address the broadest set of use cases across even the most complex technology environment.

Now I'll share a few customer wins from the quarter. The first is a Fortune 50 company that wanted to replace its existing identity system with a cloud-based identity solution that would support its hybrid environment while also deploying a Zero Trust security strategy. It was 1 of our largest contracts ever and covers Okta workforce products for over 400,000 global employees and contractors with secure access to hundreds of cloud and on-prem applications as well as Okta customer identity to improve access to its partner portal. Deploying Okta will also provide visibility of application usage and reduce IT friction by automating the provisioning of cloud applications.

Next, American Century Investments, a leading global asset manager, was a new customer identity win. The company chose Okta to replace its legacy customer identity system with a cloud-based identity platform that will provide both authentication and step-up authentication for its retail website and mobile application. The company selected Okta's customer identity products to provide a seamless and secure registration and login experience for its over 600,000 customers.

A great upsell was with the French company, ENGIE, a Global 500 multinational electric utility. This upsell is a fantastic illustration of how customers are expanding their relationship with Okta to help solve both their workforce identity and customer identity needs. ENGIE first adopted Okta's workforce identity products to support its cloud-first strategy and quickly deliver a scalable, reliable infrastructure that facilitated collaboration among its employees. This quarter, ENGIE purchased an array of Okta's customer identity products to accelerate its digital transformation for the users of its large B2B customers. Going forward, Okta will be the identity standard across all ENGIE business units.

And finally, while we just launched Advanced Server Access a few short months ago, we've already had some notable wins, including an upsell with Discovery, a Fortune 500 entertainment company with a global portfolio that includes Discovery Channel, HGTV, Food Network, TLC, Eurosport and GOLFTV. It's a great example of how our new products help expand our use cases with existing customers. Discovery first adopted Okta to serve its diverse mobile workforce and support its cloud-first initiatives. This quarter, Discovery purchased Advanced Server Access to help protect its infrastructure and extend the seamless authentication workflows to Linux and Windows machines.

We believe that great customer wins like these are just the tip of the iceberg, and that's why we are making a concerted effort to focus our energy on winning the world's largest organizations. Companies are recognizing that their success depends on their ability to quickly and securely adopt the best technologies for their workforces and customers. Every company needs to become a technology company, and we've built the Okta Identity Cloud to enable that transition with the speed, scale, security and flexibility that our customers require.

A good indicator of our progress with winning the world's largest organizations is the overall strength and 68% growth in total RPO. This is evidence that our deal sizes are getting larger and the contract term lengths are getting longer. In fact, when looking at the top 25 contracts booked in Q2 by total contract value, the average contract size doubled when compared to Q2 last year. While that's great progress, we still have a significant opportunity to further expand our business with these large organizations.

Winning the world's largest organizations continues to be an important part of our overall strategy, and we remain focused on expanding our platform to better serve them. To refresh what I've talked about before, we are focused on building products and features that can leverage more integrations. Doing so unlocks more use cases, attracts more customers and generates more data insights that can be harnessed to build better products that make our customers more successful. It's a virtuous cycle where more customer success translates to more customer wins, which translates into more customer success and so on.

So we're winning more customers. Now let's talk about the products that are increasing the use cases with our customers. Last quarter, I talked about a number of new products and features that we introduced at Oktane. We are transitioning our offering from products to a componentized platform, and the investments that we have made in this area are really starting to bear fruit. We've opened up the platform into customizable blocks that enable unlimited use cases with the Okta Identity Engine. We've introduced new functionality to our customer base like extensibility with Okta Hooks. We've also added new products like Okta Advanced Server Access to secure access to critical infrastructure and Okta Access Gateway to extend the Okta Identity Cloud to on-prem apps. These are all great examples of how we are creating the preeminent platform to help customers successfully adopt any technology. We are still in early days with each of these, but we're very encouraged by the level of interest we're seeing in these new enhancements and products, especially with our large enterprise customers like Discovery that I mentioned earlier.

We look forward to sharing more of this new product momentum as well as some additional enhancements we're making to the Okta platform at a new customer event called Okta [Showcase] on October 10 in San Francisco. Please stay tuned for more details on that event.

The last thing I'd like to say before I hand it over to Bill is that we're very pleased to be recognized as a leader by the analyst community for our vision, strategy and ability to execute. Earlier this month, Okta was once again named the leader in Gartner's Magic Quadrant for Access Management. Okta defined this category, and we've been the leader since this quadrant was created. You really have to see the graphic where we're placed in this year's Magic Quadrant because it's absolutely striking and serves as validation that we're pulling further ahead from the competition.

This recognition of our sustained leadership comes on the heels of Forrester Research recognizing Okta as a leader in their Identity as a Service for Enterprise Support. We value this recognition by the industry analysts because what it really means is that our customers are having great success with Okta and have the confidence to reference us with the analysts.

With that, I'll summarize by saying it was a very strong quarter for us driven by continued execution and market momentum. We are seeing great traction on all fronts and remain focused on capturing the massive opportunity in front of us. Thanks again for your time, and now I'd like to turn the call over to Bill to walk through our financial results. Bill?

William E. Losch - *Okta, Inc. - CFO*

Thanks, Todd, and thanks again to everyone for joining us. I'll go through our results for the second quarter and then discuss our business outlook for Q3 and the full year. As Todd mentioned, we maintained the strong momentum we had exiting Q1 and experienced strength across the board with better-than-expected growth in many areas, including revenue, calculated billings and RPO.

Total revenue was $140 million, an increase of 49%, driven by 51% growth in subscription revenue. Subscription revenue now represents 94% of our total revenue, up from 93% in Q2 last year. Revenue from outside of the U.S. grew 45% and represented 16% of revenue, which is consistent with Q2 last year. We continue to view our international business as a long-term opportunity and are investing strategically to expand our international footprint.

Total calculated billings grew 42%, and current calculated billings increased 44%. The strength in billings continues to be driven by both new and existing customers across enterprise and commercial. Billings also benefited from stronger-than-expected bookings within the quarter.

Total RPO or backlog, which for us is contracted subscription revenue both billed and unbilled that has not yet been recognized was $914 million, representing a growth of 68%. As Todd mentioned, the exceptional growth in total RPO reflects the success we've been experiencing with large enterprise customers where the contract tends to be much larger in total contract value and longer in length, up to 5 years in some cases. As we continue to see success with winning the world's largest organizations, we expect the average contract size and term length to trend upwards over time.

Current RPO, which represents subscription revenue we expect to recognize over the next 12 months, also experienced strong growth of 52% to $461 million. As I mentioned last quarter, RPO should be viewed as an additional metric to gauge our performance in the quarter. Year-over-year growth in current RPO is the more meaningful metric when viewed along with subscription revenue and billings growth. Billings can sustain variability caused by changes in invoice duration and invoice timing, while RPO can reduce some of the variability seen in billings because it eliminates variances in these invoice dynamics. However, RPO can be influenced by factors such as contract duration and renewal cycles.

Turning to retention. Our dollar-based net retention rate for the trailing 12-month period remained strong at 118% and represents a 1 point sequential decrease. The slight decrease is as expected. It is impacted by the large initial deal sizes we're achieving with large enterprise customers. As I mentioned last quarter, the net retention rate may fluctuate a bit from quarter-to-quarter. We expect it to remain very healthy as we continue to experience growth in initial deal sizes.

Before turning to expense items and profitability, I would like to point out that I will be discussing non-GAAP results going forward. Turning to gross margin. Subscription gross margin was 82.6%, up 230 basis points; and total gross margin was 77.2%, up 390 basis points. Gross profit grew 56%.

Now looking at operating expenses. Total operating expenses for Q2 grew 34%. Consistent with prior quarters, the increase is primarily driven by sales and marketing investments as we look to capture more of our large addressable market with more of the world's largest organizations and expand geographically. The overall expense growth aligns with the commitment we've made to invest in our strategic priorities, which include driving business with the world's largest organizations, strengthening the network effects of our platform, expanding our presence with customer identity and investing in security with the Okta Identity Cloud.

As usual, the biggest component to the spend increase is related to scaling headcount to support these strategic initiatives. We've been successful in attracting and retaining great talent, and total headcount grew 40%. We continue to invest in our business as we scale [durable] growth. Operating loss in the second quarter narrowed to $10 million or a margin of negative 7% compared to negative 20% in the same period last year. This is better than expected and primarily driven by our revenue outperformance. The timing of Oktane, which was held in Q1 this year versus Q2 of last year, also benefited the year-over-year compare and operating margin this Q2. Net loss per share was $0.05 with 115 million basic shares outstanding as compared to a net loss per share of $0.15 with 107 million basic shares outstanding in Q2 last year.

Turning to cash flow. Operating cash flow was negative as expected due to typical seasonality. Operating cash flow was negative $1.1 million or a margin of negative 1% compared to negative 6% in Q2 last year. Free cash flow was negative $4.3 million. Free cash flow margin improved to negative 3% compared to negative 12% for Q2 last year. We continue to expect to end the year with positive free cash flow and also expect to see continued variability in cash flow margins due to ongoing fluctuations in working capital, the growth in enterprise business and seasonal factors. We ended the second quarter with $557 million in cash, cash equivalents and short-term investments.

Moving on to our business outlook. We remain optimistic about the current demand environment; and based on our strong second quarter results, we are raising our full year outlook. Consistent with our approach throughout this year, we're using this opportunity to reinvest the upside we're experiencing in investments to innovate our platform, fuel growth and further enhance our competitive positioning. As a result, while we increased our profitability outlook for the full year, we've adjusted our Q3 outlook to invest some of our better-than-expected Q2 profitability.

For the third quarter, we expect total revenue of $143 million to $144 million, representing a growth rate of 35% to 36%; non-GAAP operating loss of $17.5 million to $16.5 million; non-GAAP net loss per share of $0.13 to $0.12 assuming shares outstanding of approximately 117 million.

For the full year fiscal '20, we are raising our guidance and now expect total revenue of $560 million to $563 million, representing a growth rate of 40% to 41%; non-GAAP operating loss of $64 million to $62 million; non-GAAP net loss per share of $0.44 to $0.42 assuming shares outstanding of approximately 116 million.

In summary, we had another strong quarter and we are looking forward to building on this momentum in the second half of the year. We are uniquely positioned to capitalize on the tailwinds and extend our leadership in the market. We've achieved great progress over the past several years, and we believe we're just getting started. The investments we're making today will help propel our future growth and solidify Okta's position as the standard for both workforce and customer identity. We are encouraged by the progress we've achieved and look forward to capitalizing on the tremendous market opportunity in front of us.

With that, Todd, Frederic and I will take your questions. Operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)And we will go first to Heather Bellini with Goldman Sachs.

Heather Anne Bellini - *Goldman Sachs Group Inc., Research Division - MD & Analyst*

I wanted to ask if you could talk about -- a little bit about just the competitive environment and maybe share a little bit given the cloud native heritage of Okta, if you could share a little bit about how customers are starting to react to your product that also can be deployed on premise and kind of how you see that, how you see that playing out and how you see -- if that changes any of the competitive dynamics further out there today. And then I have a follow-up.

Todd McKinnon - *Okta, Inc. - Co-Founder, Chairman & CEO*

The -- cool. Yes. This is a good question. It's really important part of how we think about the world. The major competitive dynamic really for the last several years has been is the company moving to the cloud or are they not. And when a company's moving to the cloud, we do very, very well. And the good news for us is that every organization, every industry is moving to the cloud. And we're very differentiated between -- we're very, very, very differentiated between most solutions because they weren't built in the cloud. They weren't preintegrated to thousands of services. They can't be upgraded. They can't be continuously connected to everything in the company's environment. So that's something we've benefited tremendously from.

We added a product that you're referring to, I think, Heather called Okta Access Gateway. We announced that at our conference back at Oktane. And really, what that does is it's a bridge to help those customers move a little bit faster over to the cloud. So it connects Okta back into their on-premise environment, gets more of their on-premise environment connected to Okta more easily and really accelerates that journey into the cloud. And it's still early for that product, but it's off to a very strong start. And we're seeing early success with it, and we're expecting big things over the next months and years.

Heather Anne Bellini - *Goldman Sachs Group Inc., Research Division - MD & Analyst*

Great. And then just a follow-up for Bill. Bill, if you would share with us, I mean you had very strong RPO growth this quarter. Just wondering, from a demand respective, there's been some concern of late just of a slowdown in the overall macro environment, and obviously, you guys are still in hyper growth mode. But have you guys noticed any change in sales cycles or anything that might make you think that the environment's a little bit more challenging than it was, say, 3 months ago?

William E. Losch - *Okta, Inc. - CFO*

Yes. Heather, we're not seeing any of those type of things. We're seeing very strong macro demand for our product. We're feeling like because these tailwinds that we have been enjoying for a while now moving to the cloud, companies digitally transforming themselves, focusing on security, these tailwinds we will -- we think are going to continue to remain C-level priorities. And as a result of that, we're feeling that, from a demand standpoint, demand is very strong for us.

Todd McKinnon - *Okta, Inc. - Co-Founder, Chairman & CEO*

Yes. One thing about the quarter too -- I'd just add to that, Heather, one thing about the quarter too is it's very balanced in terms of like success across the board. Whether it was geographically or segments of our business or the federal business, it was very balanced. So there wasn't underperformance in one area. It was covered by another area. Overperformance was very balanced across the board success.

Operator

We'll go next to Jonathan Ho with William Blair.

Jonathan Frank Ho - *William Blair & Company L.L.C., Research Division - Technology Analyst*

Congrats on the strong results. I just wanted to start out with maybe getting a little bit more color. When you talked about some of the outperformance on the larger deals, can you give us a sense of what that's being driven by? Is this mainly cross-sell or upsell, further penetration, multiproduct deals? I just think it'd be a little bit helpful to just understand a little bit what maybe some of the stronger drivers were.

Jacques Frederic Kerrest - *Okta, Inc. - Co-Founder, Executive Vice Chairperson & COO*

This is Frederic. Thanks for the kind words. As you mentioned, we're very excited about the traction that we're seeing with the world's largest organization, and that overall strength in the RPO indicates our progress there. The deal sizes are getting larger, and those contract lengths are getting longer. In fact, if you looked at the -- a piece of data, the top 25 contracts booked in Q2 by TCV, as Todd mentioned, compared to last year and that average size of contracts have doubled. And so what you're really starting to see is more and more large organizations that are either adopting the cloud and thinking about how they're going to do that internally for workforce or for their customer identity management. Good example is that Fortune 50 new customer of ours. That was entirely a workforce deployment. They're thinking about Zero Trust and how they put that strategy in. You see a lot of upsell, so the example that we talked about with ENGIE, where they've been a strong workforce customer for a long time and are now seeing opportunity to use customer identity and access management. But what has really happened over the last couple of years is with so much innovation not only in the platform but in the different products and introduction of new products, you're also seeing that we can continue to land in new places across these large organizations. So for example, a new Fortune 500 win for the quarter was with Pacific Life, brand-new customer for us and that started in customer identity management, where they wanted to do some new portals for a new type of customer. So that's a new place where they're looking for innovation in a certain way and with the breadth and depth of the Okta Integration Network and the Identity Cloud, we can really address a lot of those complex use cases now.

Todd McKinnon - *Okta, Inc. - Co-Founder, Chairman & CEO*

Yes. And I'll just add to that. The largest organizations have -- first of all, they have a lot of things we can help them with. There's a lot of complex technology. It's a very -- there's a lot of friction in adopting technology there, and we can help through that and speed their time to value across the board. But not only are the initial deals large, but there's a lot of white space too over time because they have so much need. So we're not only just excited about the size of the deals initially, but we're excited about the potential to grow in these accounts over time.

Jonathan Frank Ho - *William Blair & Company L.L.C., Research Division - Technology Analyst*

Got it. And then just as a quick follow-up, you guys have talked a little bit about the server access product. I'm just wondering, particularly as it pertains to the public cloud, have some of the recent breaches maybe lead to more inbound interest. Or is there any potential to benefit from some of the concerns out there?

Todd McKinnon - *Okta, Inc. - Co-Founder, Chairman & CEO*

There's a lot of interest in the product, and it's particularly strong in more modern development shops, where they're doing dev ops, processes, and they're being really agile in how the iterate and get code out. And that's where you've seen some of these breaches happen. And people are moving so fast and trying to innovate that sometimes they don't lock down the servers or lock down the S3 buckets like they should. So Advanced Server Access is a great fit for that. It fits into these modern software development processes, and it can help close down some of these security risks. Whether it's shared administration credentials, servers using weak passwords, user accounts not created to maintain on the servers, we can help sure that up, and it's a great fit in this modern software development world.

Operator

And we'll go next to Alex Henderson with Needham.

Alexander Henderson - *Needham & Company, LLC, Research Division - Senior Analyst*

Just one quick question on the deal length. So when you sign a 5-year deal, I assume that you're not providing any incentives for longer-term deals that you're in fact basically just extending it at their desire as opposed to incenting that. Is that correct?

William E. Losch - *Okta, Inc. - CFO*

Yes, that is correct. I mean what we're finding is the larger enterprises, because they're looking to Okta to really be the secure and scalable identity standard for them across their complex hybrid environments, are really looking for that long-term partnership with us, where we can address use cases now, we can address use cases as they evolve for them. So they're really the ones driving the length of the contracts from the standpoint that really for them is a deep partnership over time.

Alexander Henderson - *Needham & Company, LLC, Research Division - Senior Analyst*

Great. I just want to make sure that was accurate. The primary question I wanted to ask is around the Oktane pipeline. I continue to be incredibly impressed by how many people show up for that conference, and my sense is that it's delivered a substantial pipeline of leads that you are now running down. Could you give us some sense of what your lead book looks like at this point and how long it takes to close the leads that were generated from that trade show?

Todd McKinnon - *Okta, Inc. - Co-Founder, Chairman & CEO*

I don't have those numbers. I do know that Oktane is tremendously influential both for existing customers that are learning about the breadth of the platform. One of the big things we try to do and keep in mind at Oktane is that our product and our platform are very broad. And we really need to make sure we spend a lot of effort there telling our customers about the breadth of it, so they know the value can provide. So that's an important part of it. And then there's a lot of new prospects there too that are just learning about the story for the first time and we try to -- we make sure that we convey the message or the value the core product can provide in addition to explaining the breadth of the product. The -- we do see every year, we see a lot of impact on the marketing funnel and on the sales results from Oktane, which is one of the reasons why we continue to grow and invest in that event. It is a very strategic event for us. So we're happy with how it went this year, and we're happy with the -- we're confident that it's going to have a positive impact again.

Alexander Henderson - *Needham & Company, LLC, Research Division - Senior Analyst*

One last quick question if I could. The Ping filing, they're obviously setting to go public. How often do you run into Ping? How do you see them competing? Can you give us any color around what they might say or how you might position against them?

Todd McKinnon - *Okta, Inc. - Co-Founder, Chairman & CEO*

It's -- so I talked earlier about the world is really separated into legacy and the cloud future, and the best thing that's happened to us over the last 5 or so years is that everyone in the world now they know they want to -- they're either in the cloud or they want to get to the cloud. That's the future strategic direction. And I think that the competitors we see are mostly in the legacy bucket. They're software companies. They're part of a major suite of products like the IBM identity products or the computer associates, or maybe they're a stand-alone niche vendor like Ping, but they're all legacy on-premise software. And I think the market has basically decided that cloud is the future, and that's why you see our results twice the size growing twice as fast as someone like Ping.

Operator

We'll go next to Sterling Auty with JPMorgan.

Sterling Auty - *JP Morgan Chase & Co, Research Division - Senior Analyst*

So Todd, you mentioned kind of the change to the packaging and -- of products and the componentized nature of it. What does that do to pricing and how the procurement process actually works relative to how you had it structured previously?

Todd McKinnon - *Okta, Inc. - Co-Founder, Chairman & CEO*

The -- turning the products into a componentizable platform is really about addressing more use cases, so it's giving the customers the flexibility to use Okta very seamlessly for use cases that may have been difficult before or maybe not possible before. And so I really -- it's not like a repricing. It's making sure that the platform and the products can be used for every use case the customer has, whether it's maybe they just want to use a very small part of our multi-factor authentication infrastructure to get started, right? Or maybe they want to do a scenario where we do the authentication but they rely on third party to do the address and identity verification and proofing, right? It's all of those use cases that are addressed by what we call the identity engine that make it really powerful. So it's basically more flexibility, more power to address more use cases, which means more users and more products sold.

Sterling Auty - *JP Morgan Chase & Co, Research Division - Senior Analyst*

All right. Excellent. And then one follow-up. I missed if you said it on the competitive landscape. With that server access solution, what do you see in terms of head-to-head competition if there is an RFP? Or what is the other alternative that customers are considering before they actually purchase your solution?

Todd McKinnon - *Okta, Inc. - Co-Founder, Chairman & CEO*

Yes. It's a great question. Really it's -- we're competing with bad security. So we go into an environment and if they have shared admin credentials, they're not -- they're using one admin account across all their operators or all their engineers. We can go in there and put a fine-grain access control, very easy, very flexible, works in all of the dev ops workflows that, that company has. So it's really that evolving modern development and dev ops environment is really green field. It's not -- we don't -- we're not competing with people like CyberArk or some of the other PAM products. Those are more for the traditional IT PAM workloads, and we partner on those. We're really focused on more of a modern development dev ops type workflows.

Operator

And we'll go next to Melissa Franchi with Morgan Stanley.

Hamza Fodderwala - *Morgan Stanley, Research Division - Research Associate*

This is Hamza Fodderwala in for Melissa Franchi. I wanted to follow up on the macro question. Obviously, that's top of mind for companies and investors. I know it's still early days outside the U.S. but did notice that the international revenue growth decelerated quite a bit versus 60% year-on-year in Q1. Anything to read into there whether it's currency or underinvestment? Yes. Then I have a follow-up.

William E. Losch - *Okta, Inc. - CFO*

Yes. I mean the international growth remains strong. One of the things you have to think about is the outperformance of the U.S. So as a percentage of the business, it remained consistent. So it is still very strong. I think the comments I made earlier on the macro environment, that's worldwide as far as demand for us. We still believe that given the key things that we're benefiting from, these key tailwinds that we're having of companies moving to cloud, transforming themselves digitally and focused on security is true both here in the U.S. and outside the U.S., and they're going to be, we believe, high C-level priorities. In addition to that, when we talk about the success we're having in the world's largest organizations, we are talking about world's largest organizations. So we are seeing success outside of the U.S. Todd mentioned one of those companies being ENGIE in Europe, so we're seeing very strong demand across the board.

Hamza Fodderwala - *Morgan Stanley, Research Division - Research Associate*

Got it. And just to follow up, the -- could you help us square maybe -- billings growth came in around 42%, current RPO and subscription were above 50% year-on-year. Is that just duration? I know that there was some early renewals in Q1 as well, if you could help us sort of understand the some puts and takes there.

William E. Losch - *Okta, Inc. - CFO*

Yes, sure. So we do think that -- and we said this in the last couple quarters that current RPO is a very meaningful metric when you view it with billings growth. Our current RPO did grow 52%, and the reason we think it's a meaningful metric in conjunction with looking at billings is for really the reasons you just said, which is RPO, current RPO really eliminates some of that timing that you'll see with invoices, invoice timing and invoice direction and actually is a good metric to look in conjunction with billings because it eliminates that type of timing that we did see over the Q1, Q2 period.

Operator

We'll go next to Francois Yoshida-Are with Berenberg Capital Markets.

Francois Yoshida-Are

I'm on for Josh, Joshua Tilton. I believe until now the large enterprise businesses have mostly been direct. Can you just comment on what contribution from partners and specifically system integrators was driving enterprise business this quarter?

Jacques Frederic Kerrest - *Okta, Inc. - Co-Founder, Executive Vice Chairperson & COO*

Yes, happy to do that. So I mean we're seeing that the investments we were making in the partner channel continue to pay off. We're investing those both domestically and internationally especially as we find more global reach and scale. It's going to be an important part of our strategy. You talked specifically about the system integrators like Deloitte, Accenture and PwC as examples, continue to be very strong partners of ours. The reality is when you talk about the world's largest organizations, they always have relationships with at least one, if not, all of those in different parts of the organization. All of those large system integrators are thinking about how they can both enhance the identity practices and enhance the security posture of their customers, but they're also thinking about how they can help them build digital transformation practices too. That's what Accenture, Deloitte, PwC think about. Conveniently, the Okta Identity Cloud becomes so strategic that we can help them with both of those things, both helping their customers become more secure, adopt the cloud more easily but also as they think about enhancing their relationships with customers and partners and vendors. So those partnerships are going very well. We've had strong continuous support from them at the conferences and events that we go to as well as the number of employees of theirs that are getting trained and certified on the Okta service continues to grow very fast. We're very excited about those partnerships, and I think there are very bright days ahead.

Francois Yoshida-Are

And just one more follow-up. As you move into the enterprise, how do we think about the competitive positioning of the product suite with single sign-on and multi-factor authentication? We think that it's going to be highly disruptive. But in regards to life cycle management, what is the demand like there? And do enterprises view that product as enough from a functionality perspective?

Todd McKinnon - *Okta, Inc. - Co-Founder, Chairman & CEO*

The competitive position in the world's largest organizations is very solid. I mean if you see -- if you take a look at the new Gartner Magic Quadrant, we're very happy with how that comes out. And that feedback in our positioning there is largely influenced by Gartner talking to the world's largest organizations, some of which with our customers already. So they're having success. They're willing to talk with our partner, and it's a really good testament to the value we're delivering.

Specific -- on specific use cases, large organizations have -- they have many, many use cases. It makes sense, right? And they have single sign-on use cases, multifactor use cases, life cycle management use cases, and we're working across the board to make the products, continue to enhance the products and make sure that they're more flexible, more ability to address every use case, and that goes across the board to all the products whether it's single sign-on, multifactor, life cycle management. And I talked earlier about the Okta Access Gateway, which really is a way to -- it's a gateway to help these large organizations move from on-premise to where they all want to go, which is the cloud. It's like their bridge to the cloud, and it's a way for them to connect Okta back into that legacy infrastructure and keep it integrated as they move it. So we're focused on making the product. Even though they are by far the leaders in the industry, we're focused on making them even better because there's a lot of value we can deliver across the board.

Jacques Frederic Kerrest - *Okta, Inc. - Co-Founder, Executive Vice Chairperson & COO*

Two things I would add to that are, the first, as we mentioned in the prepared remarks, that Fortune 50 new customer of ours. And one of the big things they were looking for specifically was around reducing IT friction by automating the provisioning of applications so that speaks specifically to their life cycle management interest. And then in addition to that, as we discussed, our new workflows capabilities are going to continue to strengthen the end-to-end use case we can provide for large organizations for automating multi-application, multi-step workflows, HR as a master, employee onboarding and offboarding. There's just a lot of opportunity there, and we're very excited to provide that value for large organizations.

Operator

We'll go next to Andrew Nowinski with Piper Jaffray.

Andrew James Nowinski - *Piper Jaffray Companies, Research Division - Principal & Senior Research Analyst*

Congrats on a great quarter. You talked about getting into more large enterprise deals, which contributed to your RPO growth. Can you just give us any color on the large enterprise customers and how they're using the product relative to internal workforce versus external customers? Really just wondering if that mix is different in those large deals versus your historical customer base.

Jacques Frederic Kerrest - *Okta, Inc. - Co-Founder, Executive Vice Chairperson & COO*

Thanks, Andrew, for the comments. Yes, absolutely. Happy to talk about that. I think what you're seeing is that there are more and more opportunities for us to help large organizations. Think about again these 3 macro trends they're addressing. So whether it's trying to reduce cost and accelerate with the cloud, whether it's enhancing security, whether it's trying to accelerate their revenue streams and think about growing their business using customer identity and access management, you're really seeing them use more and more components of the platform in both of those use cases, both the workflow -- or sorry, workforce and customer identity management. So there's nothing significantly different than what's happened in the past. We have had large organizations as customers for some time. I think what is exciting as all the new ways that they are able to find value quickly with specific parts of the organization and the application suite and then grow from there. A good example is we put out a commentary today about Cengage, large customer of ours, one of the largest providers of learning, digital learning for university students. They have been a customer of ours just for a couple of quarters, and within 6 months they were able to deploy customer identity and access management to tens of millions of students for the new fall quarters and fall semesters in college that are just starting right now. So I think that time to value and that speed to market is something that is very attractive. And the fact that we can help them get started quickly, find success, find value and then grow with us I think portends well for the times ahead.

Andrew James Nowinski - *Piper Jaffray Companies, Research Division - Principal & Senior Research Analyst*

That's great. And then maybe just one follow-up. Your new customer add, the 450 were very strong again, but it is surprisingly consistent over the last 5 quarters regardless of the seasonality of the quarter. I'm just wondering as you -- why is your new customer growth perhaps not increasing or accelerating considering you're getting into these more -- more of these large enterprise customers and a relatively new segment now.

William E. Losch - *Okta, Inc. - CFO*

Yes. I mean you're right. The 450 customers, it is a fairly consistent growth we have every quarter between 400 and 500, and it has remained in line with that historical trend. What I'd point to is really the larger enterprise, the significant growth that we continue to have in the large enterprise. We grew 46% year-over-year in the greater than 100,000. But even more than that is the fact that we're -- with these new customers is -- the larger enterprise customers, we're doing bigger deals and we're doing longer term lengths. That's reflected in the 68% growth rate on the RPO that we talked. It's also reflected in the metric we've been talking about where the 25 largest contracts we booked this quarter were double what we booked last quarter. And so as we think about the business, obviously where we're focused on is adding new customers, but we're also focusing on adding those large enterprise customers as we talked about winning the world's largest organizations. And we're seeing a lot of success with that with larger deal sizes, longer contract lengths and overall value.

Operator

We'll go next to Gray Powell with Deutsche Bank.

Gray Wilson Powell - *Deutsche Bank AG, Research Division - Research Analyst*

Just a couple. So I know there are a lot of metrics that focus on -- and maybe I'm oversimplifying things. But if I look at the absolute dollar growth in subscription revenue in Q2, it almost doubled off the pace of Q1. So can you talk about the main driver there? And how much of that's just normal seasonality versus improved sales productivity and execution in the quarter?

William E. Losch - *Okta, Inc. - CFO*

Yes. I mean I think that what we're seeing really is all being -- not all being but primarily being driven by, again, the business that we continue to traction, we continue to see with the large enterprise. And the fact that when you see the metrics that we've been talking about specific to RPO, where the long-term RPO, the total RPO, that's -- from a growth, that actually accelerated. The growth of the current RPO accelerated quarter-over-quarter. All of those things because were larger contract lengths or longer contract lengths, much larger value is really what's driving what you're seeing.

Gray Wilson Powell - *Deutsche Bank AG, Research Division - Research Analyst*

Got it. That's helpful. And then just on the product side really quickly, how should we think about the opportunity with the Advanced Server Access products? I know it's early. But for the customers that have signed up so far, what kind of uplift are you seeing on the overall build of Okta?

Todd McKinnon - *Okta, Inc. - Co-Founder, Chairman & CEO*

It's -- the -- great. It's a good area to drill into and understand. It's something we think about a lot. We -- the product was made generally available just a few months ago at Oktane, and the early success is very positive. It's both selling it to new customers, a new way to land and also expansion in existing customers. It's -- we had a lot of success with -- as I mentioned before to a previous -- I answered a previous question to companies that are really doing modern agile development and most often, with using Infrastructure as a Service, where they deploy the software. And I think long term what we get very excited about is that is the future of software development. And the early indications are strong, but over time, we're hooked onto another major macro trend there. And as we've seen in our other businesses, building a product that is in the right place at the right time on a big macro trend like cloud or digital transformation or security is a powerful place to be. So we're very excited about that one.

Operator

And we'll go next to Gregg Moskowitz with Mizuho.

Gregg Steven Moskowitz - *Mizuho Securities USA LLC, Research Division - MD of Americas Research*

Congratulations on a good quarter. Most of my questions have been asked. But Bill, I was wondering if it were possible to provide a little more color on how much your average contract duration changed this quarter on a year-over-year basis as well as what your expectations are around duration over the next 2 quarters or so.

William E. Losch - *Okta, Inc. - CFO*

Yes. Gregg, So we've -- our average contract duration has been in the 2- to 3-year range. Because of what I said earlier, as far as these large enterprise customers and what was driving the RPO with longer contract lengths, that is ticking up within that range. I think we believe that as long as we continue, which we do believe we will continue to win more and more world's largest organizations that, that average contract length will tick up over time.

Gregg Steven Moskowitz - *Mizuho Securities USA LLC, Research Division - MD of Americas Research*

Okay. That's helpful. And then just as a follow-up, if you look at headcount, it again grew about 40% year-over-year. Do you continue to expect the hiring growth rate to accelerate in the back half?

William E. Losch - *Okta, Inc. - CFO*

Yes. So when you -- as we talked about or as I said in my prepared remarks, we saw upside in Q2 primarily driven by revenue upside. We're going to make -- take that upside and invest it later in the second half of the year primarily in Q3. Those additional investments will primarily be in customer facing headcount and innovation and headcount-related innovation, so our expectation is the growth in headcount will accelerate in the second half of the year.

Operator

We'll go next to Keith Bachman with Bank of Montréal.

Keith Frances Bachman - *BMO Capital Markets Equity Research - MD & Senior Research Analyst*

I was wondering if I could ask about the market segments. In particular, if you think about employee versus customer, could you give us any dimensions on growth rates between the 2 segments, how you really see this unfolding over the next couple of years in terms of what's being a larger TAM in terms of incremental opportunities and then how you see the pricing variances between the employee and the customer segment?

William E. Losch - *Okta, Inc. - CFO*

So the workforce market or what we call the workforce identity is still and continues to be our largest piece of our business and continues to be very strong. The customer identity also contributes to incremental upside growth and is also growing well. We think that the addressable market on both those markets is very big, which is what's exciting for us in many ways because we're 1 platform which services those 2 markets, and so there's a lot of synergies between those 2 that allows us to do a lot of upsell and cross-sell with our existing customers and with potentially new customers when it comes to workforce moving them then to customer identity and vice versa. So we feel really, really positive about that. I think from the standpoint of pricing, just from an overall pricing structure, workforce is based on a named user pricing structure and customer identity is based on an active user pricing structure just because of the different nature of the users. But like I said, we think that they're both big opportunities for us and feel good about our ability to grab those opportunities.

Todd McKinnon - *Okta, Inc. - Co-Founder, Chairman & CEO*

Okay. One thing that's missed -- I was just going to say real quickly, one thing that's missed in the competitive conversation a lot of times is that we're the only company that has scale in both of those businesses. So we're very differentiated if you -- like going back to the Gartner report, one of the things they found is that customers really value a vendor that can provide both of those. So we're very excited about both, and really we're excited about the ability to offer both because it means we can land in a more variety of ways, we have more upsell avenues, which is an important part of our strategy.

Keith Frances Bachman - *BMO Capital Markets Equity Research - MD & Senior Research Analyst*

Okay. Well, that actually was my follow-up in terms of the competitive dynamics because Ping in the registration statement talks about a fairly meaningful size of revenues from a customer side and I just wanted to tease out a little bit. I think you answer the question. Do you see any different competitive landscape between the employee and the customer side that sounds like you don't really see a difference from your competitive landscape even if you looked at ForgeRock or Ping or yourselves or some of the legacy players?

Todd McKinnon - *Okta, Inc. - Co-Founder, Chairman & CEO*

I do think that there's like -- you see ForgeRock more on the customer side, so there is a slight difference in the competitive -- set of competitors you see. The bigger difference I think are customer identity. It's more of a build versus buy. We're educating people on the fact that there is a scalable proven solution that can solve this problem for them. They don't have to build it themselves. On the workforce side, no one builds it themselves. It's -- there's leading vendors like Okta that can do it for them. That's pretty well understood.

Operator

We'll go next to Rishi Jaluria with D.A. Davidson.

Hannah Rudoff - *D.A. Davidson & Co., Research Division - Research Analyst*

This is Hannah on for Rishi. First, just following up on an earlier question. I was wondering if you could talk about how long it takes to ramp new hires to full productivity and if you're facing any challenges with the tightening labor market.

Jacques Frederic Kerrest - *Okta, Inc. - Co-Founder, Executive Vice Chairperson & COO*

Yes. Happy to talk about that. In terms of ramping new customer facing employees, we continue to see very strong learning and development internally in the organization. Obviously, with the success that we're having in the market, customer facing or account executives talk to each other, and so we're getting better and better quality of talent every day. So that's the first thing is just when you think about who's coming to Okta and their interest level, we're certainly attracting the quality of salesperson that we were not able to do 24 months ago.

Secondly, in terms of the tightening labor market, when you think about what we're trying to do, we're trying to hire the best people across the entire organization whether it's customer facing, R&D, engineering or otherwise. Those people are always well employed. And so we are always looking for the best folks. We haven't seen any significant change in our approach or in the results. You see the very strong 40% headcount growth in the first half, and we expect that to continue strong throughout the rest of the year. And we're very excited about that.

Hannah Rudoff - *D.A. Davidson & Co., Research Division - Research Analyst*

Great. That's helpful. And then a second question. I know there's a slight decel in the dollar-based net retention rate and that was impacted by larger initial deal sizes. I was wondering if you could talk about how we should think about that going forward, especially as you continue to land larger and larger customers.

William E. Losch - *Okta, Inc. - CFO*

Yes. I mean I think as we have talked about, you're right, this was impacted by larger initial deal sizes. I think as we talked with RPO growing 68% and we're landing not only longer-term deals but bigger deals, referring back to the metric we talked about earlier where the top 25 contracts we booked in Q2, that the average contract size doubled when compared to Q2 of last year. A significant portion of those contracts were net new business, and therefore, net new business meaning large initial land. So those larger initial deals are going to have an impact. And we think that the net retention rate will continue to remain healthy like it did this past quarter at 118%, but it may fluctuate a bit further remaining at this very healthy level fluctuating in the range of up or down a few points.

Operator

And we will take our last question from Shaul Eyal with Oppenheimer.

Yi Fu Lee

Congrats on the quarter. This is Yi in for Shaul. Just 2 quick questions. One -- the first one is in terms of the larger-sized deals, what is the duration in terms of the sales cycle between the large ones as compared to the small SMB ones?

Jacques Frederic Kerrest - *Okta, Inc. - Co-Founder, Executive Vice Chairperson & COO*

Yes. That's a good question. As we've talked about the overall strength that we're seeing with large organizations, those deal sizes obviously getting larger and the contract lengths are getting longer. If you think about how strategic identity is becoming in large organizations, when they make these kinds of decisions, they're obviously making it for 3 to 5 years. And so that's what we're starting to see. And when it comes to small and medium business, it is still very important decisions. We see -- we do at least annual contracts build upfront but we see more and more multiyear contracts across all the different segments of the business.

Yi Fu Lee

In terms of like sales cycle, do you have an estimate of like the duration how long it takes the sales team to close the SMB deal versus I guess a larger enterprise deal? I guess...

Jacques Frederic Kerrest - *Okta, Inc. - Co-Founder, Executive Vice Chairperson & COO*

Yes. I mean, obviously, larger enterprise deals do take longer. Typically, there are more folks involved. It's more strategic. You have to touch more parts of the organization. Whereas in smaller organizations, frankly, there's just less folks that are involved in that decision. So it's pretty typical what you'd see in enterprise Software as a Service companies like ours.

Yi Fu Lee

Okay. Fair enough. And the last question is you mentioned about the displacement opportunity on legacy on-premise vendors like IBM as well as CA. Do you have an estimate of how many customers this opportunity can be and the magnitude of it that I guess Okta could take advantage of?

Todd McKinnon - *Okta, Inc. - Co-Founder, Chairman & CEO*

I think of -- when I think about our opportunity, I think of every company. And the problem with some of that legacy technology is it wasn't sold very broadly. It was only some of the largest organizations in the world that could spend tens of millions of dollars on an identity implementation. So wouldn't -- I think our opportunity is much, much broader than just the largest organizations in the world. Those are strategically important for us, but it's much broader than that. And I think that in terms of the desire to move away from that legacy technology in the world's largest organization, the desire is really high, and now it's up for -- it's up to us to keep executing and keep delivering a robust industry leading platform that can help those customers get there. And that's what we're focused on doing.

Operator

At this time, I would like to hand the call back over to Dave Gennarelli for any additional or closing remarks.

Dave Gennarelli - *Okta, Inc. - IR Executive*

Thanks, operator. As Todd mentioned in his opening commentary, we're going to be hosting a customer event called Showcase at our headquarters in San Francisco on October 10, and you can look for more information on that next week. We'll also be hosting a number of bus tours, and we'll be marketing in Boston, New York and Los Angeles this quarter as well as attending the Berenberg U.S. Stockpicker Conference in New York on October 3, so we hope to see in one of those events. Thanks.

Operator

That does conclude today's conference. We thank you for your participation.