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PRESENTATION

Operator

Greetings, and welcome to Tenable's Quarter 2 of 2022 Earnings Conference Call. (Operator Instructions)

As a reminder, this conference is being recorded.

I will now turn the conference over to your host, Erin Karney, Senior Director Investor Relations. Please go ahead.

Erin Karney - *Tenable Holdings, Inc. - Senior Director of IR*

Thank you, operator, and thank you all for joining us on today's conference call to discuss Tenable's second quarter 2022 financial results. With me on the call today are Amit Yoran, our Chief Executive Officer; and Steve Vintz, our Chief Financial Officer.

Prior to this call, we issued a press release announcing our financial results for the quarter. You can find the press release on the IR website at tenable.com.

Before we begin, let me remind you that we will make forward-looking statements during the course of this call, including statements relating to our guidance and expectations for the third quarter and full year 2022, growth in drivers in our business, changes in the threat landscape in the security industry and our competitive position in the market; growth in our customer demand for and adoption of our solutions; the potential benefits and financial impact of our acquisitions, including our recent acquisitions of Cymptom and Bit Discovery, planned innovation and new products and services, our expectations regarding long-term profitability and our ability to attract and retain employees and its impact on our business.

These forward-looking statements involve risks and uncertainties, some of which are beyond our control, which could cause actual results to differ materially from those anticipated by these statements. You should not rely upon forward-looking statements as a prediction of future events. Forward-looking statements represent our management's beliefs and assumptions only as of today and should not be considered representative of our views as of any subsequent date. We disclaim any obligation to update any forward-looking statements or outlook. For a further discussion of the material risks and other important factors that could affect our actual results, please refer to those contained in our most recent annual report on Form 10-K and subsequent reports that we file with the SEC, which are available on the SEC website at sec.gov.

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. There are a number of limitations related to the use of these non-GAAP financial measures versus their closest GAAP equivalents. Our earnings release that we issued today includes GAAP to non-GAAP reconciliations for these measures, and is also available on the Investor Relations section of our website.

I'll now turn the call over to Amit.

Amit Yoran - *Tenable Holdings, Inc. - Chairman, President & CEO*

Thank you, Erin.

Today, I'll discuss our strong financial performance in Q2, strong demand, and the continued progress of our Cyber Exposure management platform. With that, let me first touch on Q2 results.

We delivered strong CCB growth for the quarter at 27%, which we achieved despite the macro environment. We believe cybersecurity and specifically, Cyber Exposure management remains a top strategic focus for organizations and will continue to be a spending priority. Against this backdrop, we are also very pleased to deliver compelling top and bottom line results and EPS and unlevered free cash flow were both notably above expectations for the quarter.

Our business navigated a number of ebbs and flows during the quarter that we believe are a direct result of the complicated environment our customers are operating in. We saw a few dynamics play out during the quarter. North America delivered above expectations led by Tenable.ep platform sales. Conversely, international business in most regions did not grow as fast as we expected going into the quarter, which Steve will cover in more detail. As far as the business as a whole, deals are going through more scrutiny than they typically do. Overall demand remained strong even with increased inspection on a customer-by-customer basis.

Coming out of the quarter, there were a number of things that substantiated our conviction around our business, even in the short term. Security remains a key budget priority and a defensible spend for our customers. Customers continue to face an expanding attack surface and need to properly identify their exposure and their understanding of risk. EP is an incredibly efficient way to consume our products as customers look to a more comprehensive assessment of risk. We have seen this with the strength in EP adoption and Exposure Solutions more broadly. A great example of this was a 7-figure EP competitive takeout deal with a large international financial institution. We had another strong quarter for both large 6-figure deals and overall enterprise customer adds. We continue to see large deals entering and moving through our pipeline and our confidence in the fundamentals of our business has never been stronger.

Our ability to take advantage of this demand is a direct result of meaningful and critical investments we have made, organic and inorganic, to help our customers identify and manage their Cyber Exposure. Continuing to enhance our platform, we closed the acquisition of Bit Discovery, a provider of external tax service management, enabling us to cover and assess Internet-facing assets such as web applications, cloud resources and open gateways.

Following the closing of the acquisition, we delivered a new version of Nessus, Nessus Expert, that includes external asset discovery. External asset discovery will be included at no additional cost for our enterprise platform customers, and a separately sold context to where external attack surface management offering for continuous discovery and ongoing monitoring is also available today.

Cyber Exposure Management as a discipline is attracting attention from industry analysts and customers alike. It is an incredibly important approach to managing cyber risk and it is an approach that we've pioneered over the last several years. We believe delivering on a successful Cyber Exposure management platform requires a unified best-in-class approach across vulnerability management, cloud security, Active Directory security, OT security and other parts of the attack surface, which we are successfully executing on. We believe our roots and laser focus position us incredibly well to be a market leader.

As we continue to execute on our own vision, we're excited to see industry acknowledgments and the importance of this discipline. Continued coverage by Gartner talking about exposure management as a discipline, amplifies this point. In particular, the importance of advancing Cyber Exposure Management program adds critical to developing actionable posture improvement plans that can be understood by executives. As Boards and executives are pressured to understand their cybersecurity posture, having a clear view of risk is increasingly critical.

Preventing cyber attacks requires full visibility into all assets and exposures, extensive context into potential security threats and clear metrics to objectively measure cyber risk. Tenable's Cyber Exposure Management platform delivers visibility across the modern attack surface with intelligent analytics to prioritize preventative actions and communicate risks to all levels of the organization. We are building the broadest understanding of Cyber Exposure, spanning IT assets, cloud resources, containers, web applications and identity services. We're delivering unifying analytics, prioritized actions and benchmarking to help our customers truly manage risk more effectively. And that's a compelling capability.

I will now turn the call over to Steve for further commentary on our financial results.

Stephen A. Vintz - *Tenable Holdings, Inc. - CFO*

Thanks, Amit.

As Amit mentioned earlier, we are pleased with our results for the second quarter, highlighted by good topline growth, a sizeable beaten EPS and strong unlevered free cash flow. There are a confluence of factors related to the broader market that impacted our results, but we are pleased with our execution in the quarter despite a more cautious spend environment.

I will provide more commentary momentarily. But first, please note that all financial results we discuss today are non-GAAP financial measures, with the exception of revenue. As Erin mentioned, at the start of this call, GAAP to non-GAAP reconciliations may be found in our earnings release issued earlier today, which is posted on our website.

Now on to the results for our quarter. Calculated current billings, defined as the change in current deferred revenue plus revenue recognized in the quarter, grew 27% year-over-year to $174.1 million and benefited from our continued investment in our platform strategy and go-to-market efforts.

The fundamentals of our business remain very strong, and we are pleased with the demand overall in the quarter, but it was mixed across geographies as North America exceeded our expectations while our international theaters encountered headwinds and fell short of expectations.

As a reminder, we go to market using a 2-tier channel model with our customer contracts denominated in U.S. dollars. During the quarter, the U.S. dollar strengthened compared to other currencies, which made our products more expensive, and that, combined with other macro considerations, impacted our international sales.

In addition, on a global basis, we experienced deeper levels of inspection and more approvals with some customers. Despite that, we are pleased with our CCB growth, and had one of our best quarters in terms of adding new customers and transacting large deals. Specifically, we added 540 new enterprise platform customers and 79 net new 6-figure customers in Q2, which represents 35% and 28% year-over-year growth, respectively.

Underpinning our customer momentum is EP, Tenable.ep, which continues to see strong demand in both the large and mid-market and has resulted in more meaningful deal sizes, amplified by the addition of cloud and identity security to our unified exposure platform. Tenable.ep also creates a more compelling upsell path for our existing customers and benefited our dollar-based net expansion rate in the quarter, which remains elevated in comparison to prior years, and is well above our 110% threshold.

Revenue for the quarter was $164.3 million growth in Q2 last year. Revenue in the quarter exceeded the midpoint of our guided range by $1.3 million. As discussed earlier, we experienced less-than-expected international sales, which typically have a higher mix of stand-alone Active Directory on-premise deployments, which is our only software solution with upfront revenue recognition. Consequently, product mix limited our upside in revenue this quarter. That said, visibility remains high as our percentage of recurring revenue was 95%, which is consistent with prior periods.

I'll now turn to expenses, which include incremental investments in growth and the operating expenses related to the Bit Discovery acquisition that we closed in the quarter. I'll start with gross margin, which was 81% this quarter and essentially flat compared to last quarter. Despite increased usage of our cloud products, our public cloud costs decreased sequentially as a result of efforts to optimize the efficiency of our product delivery infrastructure, along with our procurement strategy, which resulted in credits in the quarter that reduced our compute costs. These savings were offset primarily by increased personnel costs for support of our products.

In connection with the closing of Bit Discovery, we launched a new external attack surface management offering in July that we will continue to integrate throughout our product portfolio. Also, as a reminder, we plan to release a more expansive set of Cyber Exposure analytics in the second half of the year. This will include attack path analysis, enhanced unified analytics and improved benchmarking and contextualization of vulnerabilities, all of which will help customers better visualize and efficiently manage risk across their hybrid environments.

We expect the incremental investments for Bit Discovery and Cymptom, a portion of which are upfront costs to modestly impact gross margins in the second half of the year, but provide runway to support future growth. As I've indicated in the past, long term, we still expect gross margins to be in the high 70% to low 80% range.

Sales and marketing expense for the quarter was $75.6 million, which was up from $71.5 million last quarter. Sales and marketing expense increased sequentially due to higher wages and benefits related to hiring more quota-carrying sales reps and associated head count as well as higher marketing spend related to industry and other events. Sales and marketing expense as a percentage of revenue was 46% in Q2 compared to 45% last quarter.

R&D expense for the quarter was $28.1 million, which was virtually flat compared to $27.8 million last quarter. It should be noted that we added incremental engineering head count in support of unifying our product architecture and enhancing our platform, and capitalized $2.9 million of software development costs. R&D expense as a percent of revenue was 17% in Q2, which was consistent with last quarter.

G&A expense was $17.3 million compared to $16.6 million last quarter. We continue to make investments in our back-office functions and systems to support the growth and scale of our business. As a percentage of revenue, G&A expense was 11% this quarter compared to 10% last quarter.

Income from operations was $12.2 million, essentially flat compared to last quarter, but $5.7 million better than the midpoint of our guided range, which had contemplated incremental COGS for our public cloud infrastructure, increased spend for industry events, and higher head count and related costs. However, in response to the changing business climate, we were able to achieve greater operational efficiency through more focused efforts on spend optimization, which resulted in upside to op income in the quarter. It's also worth noting that a stronger U.S. dollar contributed approximately $1 million of outperformance as approximately 40% of our employees are based outside of the U.S. In short, we incurred less expense in our international locations due to a stronger dollar.

Operating margin was 7% for Q2 compared to 8% last quarter. EPS in the second quarter was $0.05, which was $0.035 better than the midpoint of our guided range due to the same expense trends I just mentioned. EPS also includes $0.02 or $1.8 million of FX remeasurement losses included in other expense net. As a matter of clarity, this FX activity is due to the remeasurement of our non-U.S. dollar-denominated cash and other monetary assets and liabilities. The FX remeasurement losses more than offset the $1 million of OpEx savings from FX I previously discussed.

Now let's turn to the balance sheet. We finished the quarter with $510.9 million in cash and short-term investments. Accounts receivable was $109.4 million, and total deferred revenue was $548.1 million, including $415.4 million of current deferred revenue, which gives us a lot of visibility into revenue over the next 12 months.

Now I would like to discuss cash flow. We paid $3.3 million of cash interest on our credit facility in the quarter. Looking ahead, we are assuming a higher interest rate environment with our floating rate debt facility when it resets at the end of July. Consequently, our full year guidance reflects $17.9 million of interest expense, which is $2.2 million higher than our previously provided guidance. That said, our Term Loan B continues to provide a very low cost of capital, which has allowed us to fund acquisitions without equity dilution to our shareholders.

Earnings on our cash and investment balance provides a partial natural hedge to interest rate expense. As such, we expect the full year EPS impact on interest expense net of interest income to be $0.01 as yields on our cash and investments also rise.

We generated $29.1 million of unlevered free cash flow, which is an 18% margin. With 95% recurring revenue, high gross margins and renewal rates, we feel confident that we can continue to generate attractive levels of cash flow while continuing to invest in the business.

Striking the right balance between growth and profitability has always been and will continue to be an area of focus for us. Last year, we became a Rule of 40 company, and we are confident we are well on our way to becoming a Rule of 50 company.

With the results of the quarter behind us, I'd like to discuss our outlook for the third quarter and full year 2022. In terms of the topline growth, our guidance reflects a continuation of the trends we experienced in the back half of the second quarter. Specifically, we expect the fundamentals of our business and the demand for our Cyber Exposure solutions to remain strong. However, given the current macro environment, we think it's prudent to expect a similar level of review and scrutiny on some deals that we experienced in Q2.

Our guidance also contemplates approximately $4 million to $5 million of less contribution from upfront AD on-prem revenue and higher levels of adoption of AD in Tenable.ep, our unified Exposure platform. Now in terms of expenses, our outlook reflects the expected impact of inflationary costs, most notably on wages, the absorption of Bit Discovery and higher interest expense on our floating rate debt.

With that in mind, here are the specifics. For the third quarter, we currently expect revenue to be in the range of $169 million to $171 million. Non-GAAP income from operations to be in the range of $9 million to $10 million. Non-GAAP net income to be in the range of $3.2 million to $4.2 million assuming interest expense of $5 million and a provision for income taxes of $2.3 million. Non-GAAP diluted earnings per share to be in the range of $0.03 to $0.04, assuming 119.5 million fully diluted weighted average shares outstanding.

And for the full year, we currently expect calculated current billings to be in the range of $768 million to $776 million, which reflects a $4 million increase from the midpoint of our prior guidance, including $2 million of the Q2 outperformance and $2 million of contribution from Bit Discovery, primarily in Q4. Revenue to be in the range of $673 million to $679 million, which remains unchanged. Non-GAAP income from operations to be in the range of $45 million to $49 million, which is a $1 million increase from the midpoint of our prior guidance, reflecting a $6 million beat over the midpoint of our Q2 guidance, offset by $3 million of operating losses from Bit Discovery and $2 million of higher inflationary costs. Non-GAAP net income to be in the range of $19.7 million to $23.7 million, assuming interest expense of $17.9 million and a provision for income taxes of $7.6 million. Non-GAAP diluted earnings per share to be in the range of $0.17 to $0.20 reflecting the $0.035 beat from the midpoint of our Q2 guidance, offset by approximately $0.03 related to Bit Discovery and $0.01 of higher net interest expense. Our EPS guidance assumes 119 million fully diluted weighted average shares outstanding.

In summary, we're very pleased with the results for this quarter. We feel good about the fundamentals of our business and believe we are thoughtfully navigating the current climate to deliver continued growth and profitability.

I'll now turn the call back to Amit for some closing comments.

Amit Yoran - *Tenable Holdings, Inc. - Chairman, President & CEO*

Thanks, Steve.

We hope to see many of you at the Canaccord and Piper conferences in the coming weeks.

We'd now like to open the call up for questions.

QUESTIONS AND ANSWERS

Operator

(Operator Instructions)

The first question comes from Hamza Fodderwala of Morgan Stanley.

Hamza Fodderwala - *Morgan Stanley, Research Division - Equity Analyst*

Steve, for you. I just want to be really specific. So it seems like just the negatives in the quarter were international. It sounds like Europe coming in slower than expected, The higher scrutinization of deals. That was exclusively to Europe, and then FX basically making the products more expensive. Was there anything in North America or other regions that you saw that was driving that scrutinization as well? Or was it just concentrated in Europe?

Stephen A. Vintz - *Tenable Holdings, Inc. - CFO*

I would say, first of all, overall, we're pleased with our performance in the quarter. We grew CCB 27%. And as you know, we added a lot of new customers, 540 new enterprise platform customers. We transacted a bunch of large deals. So one of our best quarters in terms of momentum.

As I called out earlier, performance was mixed. We saw significant strength in North America, which is our largest theater. But international felt short of expectations for some of the reasons that you mentioned. In terms -- generally, we are seeing more levels of scrutiny in review, but we were able to overcome this because we saw strength in our enterprise business. So we're just commenting on the current environment in terms of what we're seeing. And by the way, I referred internationally, broadly, but it's more specifically in EMEA, which is what you had mentioned before. And I will say this, that it's not pervasive across all countries, right, in our international theaters and specifically in Europe, not across all countries. It's more on a customer-by-customer basis. It's based on specific company budget dynamics, industry, geo. And we saw strength in major sectors, including in Europe.

So obviously, overall, we're pleased with our results for the quarter. We're raising CCB guidance for the year, and we think we're set up for success for the second half of the year.

Hamza Fodderwala - *Morgan Stanley, Research Division - Equity Analyst*

Just one quick follow-up on that. When it comes to international, are you increasing the level of discounting for your products? And is that something that's reflected in the back half guide?

Stephen A. Vintz - *Tenable Holdings, Inc. - CFO*

No. We're not. We did not see that in the second quarter, levels of discounting increase. We're mindful of that as we enter the second half of the year, but we're spending a lot of time looking at pipelines. We feel really good about our pipelines as we head into the second half of the year, not just the size but also the shape and maturity of it. Activity levels are high, and we're looking at all forecast lenses. Spending a lot of time qualifying opportunities. We feel good about the second half of the year and our self.

Operator

The next question comes from Rob Owens of Piper Sandler.

Robbie David Owens - *Piper Sandler & Co., Research Division - MD & Senior Research Analyst*

Maybe like Hamza, I'll sneak in one as well. Would love to better understand this. The higher levels of scrutinization, I guess, juxtapose what you're seeing with your enterprise customers in large deals, the success on that front. And as we enter the third quarter, just any broad brushes around government.

Amit Yoran - *Tenable Holdings, Inc. - Chairman, President & CEO*

Yes. Thanks. Great question. I'll chime in and I'll say listen, it's just a tough macro environment. And as a result, many customers, and it's on a region-by-region basis, on a customer-by-customer basis, many customers are looking at their spend, at their expense bases, and they're scrutinizing every contract, every opportunity. Security remains top of list. We are not seeing a high level of customers abandoning their position in pipeline. Deals continue to move forward in the pipeline. There's just additional signatures to get in the process that companies are putting in place on a customer-by-customer basis. But again, pipeline continues to build at a healthy rate, has never been stronger than it is today. Deals continue to move forward in the pipeline, and we feel exceptionally confident in how we're set up going into the third quarter and going into the year.

You asked specifically about public sector. We had a good quarter in the public sector, I'd say, kind of in line with expectations, including a 7-figure transaction at the state level. Globally, public sector did really well. And we continue to invest with a high degree of confidence in the public sector, seeing strong opportunity in our pipe, seeing more transactions and seeing longer transactions than we've seen at any point in recent history. So again, we feel as well set up as we can going into the third quarter.

Operator

The next question comes from Saket Kalia of Barclays.

Saket Kalia - *Barclays Bank PLC, Research Division - Senior Analyst*

Excellent. Steve, I'll keep it to one, and maybe just for you. Can you just dig into the dynamic that you mentioned on AD a little bit for upfront revenue? I think you said it's about $4 million or $5 million less contribution this year. Can you just flush that out a little bit? Is that on revenue? Is it on CCB? And why the change?

Stephen A. Vintz - *Tenable Holdings, Inc. - CFO*

Yes. The $4 million to $5 million is on -- for AD on-prem, the second half of the year, specifically the second half of the year. So we're taking the $4 million to $5 million out of our guidance. And so we're just seeing slightly different mix. That said, we are very pleased overall with our ability to sell identity security as a stand-alone offering into our customer base. We've demonstrated success doing that, and now part of a broader offering in Tenable.ep. With regard to the latter, I think it's important to note, we've integrated AD security into EP as well as cloud security -- and we're actually seeing -- historically, we're seeing a 60% uplift in Tenable.ep, our unified Exposure Management Platform relative to our core VM offering. And we're now seeing a 70% uplift. So we're having success transacting larger deals, specifically because of EP. Certainly, AD is an important part of that. but our guidance reflects a lower contribution due to less expected AD on-prem revenue.

Amit Yoran - *Tenable Holdings, Inc. - Chairman, President & CEO*

Yes. Saket, just to clarify, the AD on-prem revenue is all recognized upfront. So it has a disproportionate impact on the quarter and our expectations for the remainder of the year.

Stephen A. Vintz - *Tenable Holdings, Inc. - CFO*

And AD is our only product that has upfront revenue recognition. Every -- all the other products are ratable.

Saket Kalia - *Barclays Bank PLC, Research Division - Senior Analyst*

Okay. So just to be clear, just to put a bow on this topic. It doesn't sound like all the CCB expectation for AD is going down in totality, just the mix of what is cloud versus on-prem. Is that right? Or are we --- the expectation?

Amit Yoran - *Tenable Holdings, Inc. - Chairman, President & CEO*

No, that is right. That's why you saw the outperformance in CCB. That's why we're -- we pass on a beat, and we're also raising in CCB. We have not raised our outlook for revenue because we're reflecting less upfront revenue related to stand-alone AD on-prem.

Operator

The next question comes from Mike Cikos of Needham & Co.

Michael Joseph Cikos - *Needham & Company, LLC, Research Division - Senior Analyst*

I just wanted to circle back to that increased route that you guys are seeing. Can you help us think through when that dynamic really started to come into play for the international markets that increased scrutiny? And maybe it would be helpful, too to talk through how that trended through the quarter through July, like deals seeing as a result of the scrutiny, are those deals extending with more constituents sitting around the table? Has that deteriorated further as we've gone from May to June to July? Or have things been relatively stable when we start thinking through that scrutiny that you guys were talking to earlier?

Amit Yoran - *Tenable Holdings, Inc. - Chairman, President & CEO*

Yes. We saw that scrutiny really kick in in June, and things have been relatively consistent since then. Again, the sales team has a lot of confidence, they continue to enter deals into the pipe, deals continue to move through the pipeline. There's just more signatures to get in order to close transactions. I don't think it's specific to Tenable. I don't think it's specific to security. I think largely speaking, we do not hear the sales team tell us the budgets are going away. We don't hear them telling us that deals are going away. It's just a matter of some transactions on a customer-by-customer basis require additional signatures. And as you note, in certain instances, that can kick -- prolong the sales cycle. But we feel exceptionally confident given the pipe and the progress through the pipe in second half of the year, and that's reflected in the increase in CCB.

Michael Joseph Cikos - *Needham & Company, LLC, Research Division - Senior Analyst*

That's very helpful. And if I could just squeeze one more in. When looking at the strength of the new enterprise platform customers added or even the customers over $100,000 in ACV at period end, you guys had some strong numbers when looking at those metrics. And I just think it would be helpful to frame out for the investment community here. But can you help us think through the segments that you guys are working through? If I think about like enterprise versus mid-market versus SMB, if I stratify your customer base according to those different parameters, we're starting to see a different behavior coming out of enterprise versus maybe mid-market. And maybe remind the 2 as far as your exposure to each of those different stratifications would be helpful as well.

Stephen A. Vintz - *Tenable Holdings, Inc. - CFO*

Yes. So as we commented earlier, we had one of our best quarters in terms of customer demand in terms of new enterprise platform customers, and large deals. So really strong. And if you kind of look, disaggregate that, we saw significant contribution from enterprise as well as commercial. Both are working well in aggregate globally for the company. Commercial, which we'll say is mid-market is certainly an area of opportunity for us. We're building out a commercial team in APAC, and we're seeing outperformance there. But overall, we saw strength in both our large and mid-market, both commercial as well as enterprise.

And of course, exceptional strength in North America. And as we commented earlier, EP is figuring prominently here. We're transacting larger deal sizes. It's covering more areas of the attack surface, and we're getting -- now getting a 70% uplift relative to our core VM offering.

Operator

The next question comes from Brad Reback of Stifel.

Brad Robert Reback - *Stifel, Nicolaus & Company, Incorporated, Research Division - MD & Senior Equity Research Analyst*

Great. Steve, with respect to the 2H guide, how should we think about what you've modeled in for international and domestic? So I think you talked about international having pockets of weakness. So are you assuming that it's just those pockets going forward? And that you just -- domestically, it's been very strong. Do you expect that strength to continue in the guide? Whatever type of moderation you've put in there would be great to highlight.

Stephen A. Vintz - *Tenable Holdings, Inc. - CFO*

Yes. I think some of the trends that we saw in the second quarter were expecting to play out for the second half of the year. I will say the secular trends of our business are very strong, and we're seeing healthy levels of demand. Now North America was strong, and we expect it to continue to be this second half of the year. Our guidance reflects not only what we experienced in Q2, but what we also saw in July. And so we're taking everything into account. We have a lot of confidence in our ability to execute. And so it's really a continuation of trends.

Operator

The next question comes from Brian Essex of Goldman Sachs.

Brian Lee Essex - *Goldman Sachs Group, Inc., Research Division - Equity Analyst*

I was wondering if you could dig in a little bit on the sales side. I mean I think you guys, last quarter, talked about elevated hiring in the front half of the year. How does that pan out? Is there any way you can parse that out by geography and level of success attracting and retaining talent where you need it? And are we looking at maybe an elevated spend in the front half of the year with better leverage in the back half of the year? Or given the current macro situation, has any of that changed at all?

Stephen A. Vintz - *Tenable Holdings, Inc. - CFO*

This is Steve. I'll start. Our hiring is an area that we called out earlier. So we are continuing to hire and invest. So significant levels of hires in the first half of the year, specifically in Q2. So we're adding quota capacity and obviously -- not just domestically but also abroad, and that's really important. Coming into the year, we increased quotas. Productivity levels continue to be healthy globally. And so my expectation in the second half of the year is that you'll see a leverage in the business, and our guidance reflects that.

So overall, we think we're striking the right balance between growth and investment. We do not want to moderate the level of investment, right, just given what we're seeing outperformance in CCB and sales. While performance may have been mixed globally across the board, across various theaters, we have a lot of confidence in our business and we expect continued success in the second half of the year. So yes, we're still continuing to lean in and invest both on the sales side as well as engineering.

Operator

The next question comes from Jonathan Ho of William Blair.

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

Can you maybe help us understand or quantify the FX impact and international underperformance on the business this quarter? And maybe what your assumptions are around guidance on the magnitude of that impact going forward?

Stephen A. Vintz - *Tenable Holdings, Inc. - CFO*

Sure. So I think Jonathan's question's around FX. I'll start and feel free to interject.

So as a reminder, our customer contracts are denominated in U.S. dollars. In terms of operating expenses, there was a $1 million benefit sequentially from the stronger dollar impacting expenses in local currency. Impact was primarily due to fluctuations in the euro and well, say the British pound. Further, the remeasurement of cash and other monetary balances in local currency, that means outside of the U.S, resulted in a $1.8 million loss, which is reflected in other income, so below the line. Average rate in Q2 was like $1.07 for the euro, $1.26 for the pound. We're expecting something similar for the second half of the year.

Amit Yoran - *Tenable Holdings, Inc. - Chairman, President & CEO*

Yes. I guess the only thing I would add to that is, broadly speaking, strong demand, including in international markets, and that's reflected in the increase in CCB and confidence in the business that you're hearing on the call, the primary discrepancy is probably the recognition of AD on-prem revenue. And so for that reason, not raising the revenue guide here. But more broadly speaking, we feel really good about the business, the rate of growth, the deals entering the pipeline and our ability to continue to move deals through the pipeline and increase CCB guide as a result.

Operator

The next question comes from Gray Powell of BTIG.

Gray Wilson Powell - *BTIG, LLC, Research Division - MD & Security and Analytics Software Analyst*

Great. And I guess before I ask it, I just want to say thanks for the transparency just on the headwinds that you're seeing in the international business. I'm not sure how long everybody -- other companies would deal with that. You may have answered this before, but just roughly speaking, can you help us think through how much the softness on the international side impacted billings in Q2? Like was it a small miss? Was it a big miss? Just any sort of order of magnitude would be really helpful there.

Stephen A. Vintz - *Tenable Holdings, Inc. - CFO*

I think it's fair to say that we would have seen a couple points of additional growth in the second quarter. So order of magnitude, we're not talking about something that's sizable. We're talking about something that's just different than what we've experienced in prior quarters. So that's why we're calling it out. And of course, they have a procurement bias towards upfront revenue, it did have an impact on revenue. So that's why we're being -- providing the transparency.

Gray Wilson Powell - *BTIG, LLC, Research Division - MD & Security and Analytics Software Analyst*

Got it. So a couple of additional points of growth on Q2 total billings, had it not been for international? Just to make sure I got that correct.

Stephen A. Vintz - *Tenable Holdings, Inc. - CFO*

Yes, I think that's a fair characterization.

Operator

The next question comes from Joshua Tilton of Wolfe Research.

Joshua Alexander Tilton - *Wolfe Research, LLC - Research Analyst*

Assuming that you had some deals slip in EMEA this quarter, have you been able to close them since the quarter closed?

Stephen A. Vintz - *Tenable Holdings, Inc. - CFO*

Yes, we have closed some of those. But obviously, it's very early in the quarter. And that's one of the reasons why we feel really good about our guidance for the second half of the year and why we're providing -- passing through the beat, and also increasing. But we also know there's more deals to close, right? And our pipeline -- we talked about the quality of the shape and the size of the pipe. There are a lot of large deals as we head into the third quarter. So we're going to continue to focus on moving these deals to the pipeline and closing deals. And obviously, we think we're set up well for success.

Joshua Alexander Tilton - *Wolfe Research, LLC - Research Analyst*

And just to maybe sneak one more in there. You said it's not -- or you don't think it's specific to Tenable, but I kind of want to ask the question a different way. From your conversations with customers, does it sound like it's a VM issue? Or is it just a broader scrutiny issue?

Amit Yoran - *Tenable Holdings, Inc. - Chairman, President & CEO*

No. I think it's just a broader scrutiny issue. And it's -- again, I don't think it has anything to do with VM. I don't think it has anything to do with security. Customers are changing their procurement processes as they look at their operating expenses. I sat with a number of CISOs over the last couple of weeks, and the security budgets are not changing but procurement processes require additional hoops in jumping and that just has added in certain instances, a number of delays to transactions that are in process.

So we don't think it's specific to VM. We don't think it's specific to security. And I don't want to say we're previous to it, but I think to a large extent, it's just deal process, not so much change in budget.

Operator

The next question comes from Rudy Kessinger of D.A. Davidson.

Rudy Grayson Kessinger - *D.A. Davidson & Co., Research Division - SVP & Senior Research Analyst*

I guess I'm curious, if you look at the increased level of scrutiny, obviously, North America outperformed relative to EMEA in the quarter. But is the increased level of scrutiny kind of similar across geographies and just more deals are getting pushed across the finish line in North America? Or just what's the dynamic there? And then secondly, if you look at the new deals in the quarter, did you have maybe some customers that started the quarter were considering maybe going with EP and then maybe the downsize their deal to maybe just going with IO. I'm curious if you saw any of that as well.

Stephen A. Vintz - *Tenable Holdings, Inc. - CFO*

No. We certainly haven't seen that. EP continues to do very well for us. It's double-digit percentage of new sales. It's higher this quarter than it was last quarter. Penetration back into our customer base, has been strong, but it's still modest in terms of the opportunity, single-digit penetration. And we're getting even more of an uplift. So absolutely not on the EP side. And you broke up a little bit the first part of your question...

Rudy Grayson Kessinger - *D.A. Davidson & Co., Research Division - SVP & Senior Research Analyst*

... in terms of North America.

Stephen A. Vintz - *Tenable Holdings, Inc. - CFO*

Again, I would just say with regard to deals, I think it really varies. Now clearly, North America exceeded our expectations, and there's just really strong momentum there. I think just generally speaking though, there are more levels of review across the board. Now the good news is we were able to overcome that. And what we don't want to lose sight of is really the bigger picture here, which is we had a great outcome for CCB. We grew 27%. Customer momentum has never been better. It's one of our best quarters for closing deals, new enterprise customers, one of our best quarters for closing large deals. We're getting uplift from EP.

So a lot of areas of our business continue to be very, very strong. We're providing just additional color commentary on how performance varied across the board because it did have an impact on revenue. But we have -- I want to make sure we don't -- we have a lot of confidence in our business. And hopefully, our guidance today reflects that. We're just providing additional color commentary for -- because we think it's necessary.

Operator

The next question comes from Mike Walkley of Canaccord Genuity.

Thomas Michael Walkley - *Canaccord Genuity Corp., Research Division - MD & Senior Equity Analyst*

Just a follow up to that with EP on single-digit penetration. How should we think about the dollar-based net retention should remain above your 110% threshold for quite some time? Or are you seeing any kind of slowdown in terms of larger deal momentum with the increased scrutiny?

Stephen A. Vintz - *Tenable Holdings, Inc. - CFO*

No. Our dollar -- I'll -- let me chime in here. But in terms of the metrics itself, which is our dollar-based expansion rate. It's very healthy, well above the 110% threshold. And as we commented earlier, it's elevated. EP certainly playing a big part of that because we're having success selling it back into the base as well as other products, too. So yes, absolutely healthy in terms of the expansion within the customer base.

Amit Yoran - *Tenable Holdings, Inc. - Chairman, President & CEO*

Yes. The only thing I would add to EP is -- as Steve noted, this 70% higher ASP. So the differentiation in ASPs as customers move to EP is actually increasing, which is a phenomenal sign and helping signal. The comment about single -- so it's a double-digit percentage of new customer growth. I think Steve's comment that it's a single-digit percentage of our existing customers that are on EP. So when you look at the size of the ASP increase in our ability and the success that we're showing going back into the base and upselling them to EP, it just speaks to the opportunity for net dollar expansion rate moving from individual products to EP as well as asset expansion.

Operator

The next question comes from Andrew Nowinski of Wells Fargo.

Andrew James Nowinski - *Wells Fargo Securities, LLC, Research Division - Senior Equity Analyst*

I don't think you guys mentioned Log4j in the prepared remarks this quarter. And I know last quarter, you talked about it potentially only having an impact in Q1, but then a few weeks ago, I think DHS put out a report that said Log4j would remain a risk to organizations for the next decade. Do you think it may have pulled in any deals into Q1? And what impact you did have in Q2? And then how are you thinking about it as it relates to your pipeline going forward?

Amit Yoran - *Tenable Holdings, Inc. - Chairman, President & CEO*

Yes. I think there's no doubt we saw some tailwind from Log4j top of mind for customers and prospects at the end of Q4 and going into Q1. Log4j will be with us for years to come. I think over time, folks will be and are integrating Log4j activities into the more standard operating pace and procedures and less of a -- there's an emergency spend. We really need to get visibility around this particular key issue. Again, it's not to say that some issue might not raise its head in the current or next quarter that would cause a similar buying behavior. But we don't -- I think it's fair to say, it means vulnerability management is strategic and will continue to be, but I don't think there's the type of urgency around Log4j procurement that we saw late last year and beginning of this year.

Operator

The next question comes from Shebly Seyrafi of FBN Securities.

Shebly Seyrafi - *FBN Securities, Inc., Research Division - MD*

Do you expect your federal and public segment business to outgrow your overall business by a larger margin in this current fiscal Q3 than, say, last year's fiscal Q3 because of the funding? And just can you provide us with an update on roughly what your current federal and public percentage of revenue is?

Stephen A. Vintz - *Tenable Holdings, Inc. - CFO*

It's approximately 15% of our total sales, and that's public sector as a whole. Going into Q3, which -- we think our pipeline has been strong. There's a lot of opportunity. So we feel good about public sector. And as Amit commented earlier, we saw areas of strength globally within public sector and specifically at the state and local level has been an area of investment for us. In our guidance, we didn't really break out growth rates by theater and what we're expecting. But I will say, we're expecting certainly a sequential uptick in sales or CCB from our public sector theater.

Operator

Ladies and gentlemen, we have reached the end of our question-and-answer session. This concludes today's conference. Thank you for your participation, and you may now disconnect your lines.

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