Dropbox

Dropbox Q3 2025 Prepared Remarks

PETER STABLER, INVESTOR RELATIONS

Good afternoon, and welcome to Dropbox's third quarter 2025 earnings call.

As a reminder, we will disclose non-GAAP financial measures on this call. Definitions and reconciliations between our GAAP and non-GAAP results can be found in our earnings release and our earnings presentation posted on our IR website at investors.dropbox.com.

We will also make forward-looking statements on this call, including statements about our future outlook for our fourth quarter and fiscal year 2025, as well as our expectations regarding our business, assets, strategies, and the macroeconomic environment. Such statements are subject to known and unknown risks and uncertainties that could cause actual results to differ materially from those described.

Many of those risks and uncertainties are described in our SEC filings, including our most recent and forthcoming reports on Form 10-Q. Forward-looking statements represent our beliefs and assumptions only as of the date such statements are made. We disclaim any obligation to update any forward-looking statements except as required by law.

I will now turn the call over to Dropbox's CEO and co-founder, Drew Houston.

DREW HOUSTON, CHIEF EXECUTIVE OFFICER

Thanks Peter, and good afternoon everyone. Welcome to our Q3 2025 earnings call. I'm here with Tim Regan, our CFO.

I'll walk through our business and product highlights, then Tim will cover our Q3 results and our outlook for the rest of the year.

Our teams executed well this quarter. Constant currency revenue came in comfortably ahead of guidance, driven primarily by better-than-expected retention across our Individual and self-serve Teams plans. Non-GAAP operating margin was up meaningfully year-over-year, reflecting our focus on operational efficiency along with some timing-related spending shifts that Tim will cover.

Now let's dive into our two strategic priorities which are scaling Dash and simplifying and strengthening our Core FSS business.

We'll start with Dash. Our industry is spending trillion of dollars on AI models that can explain quantum physics but can't find your Q2 board deck. This is the problem that we're solving with Dhas.

Specifically, the issue with today's tools is that they don't understand your context at work. Consumer AI tools don't know about your company. Copilot can't see your Slack. Gemini can't see your Salesforce. You're always starting from zero, cutting and pasting, and uploading documents one at a time. Meanwhile, SMBs are either overlooked by enterprise search tools or are stuck using consumer tools that weren't built for business and create real security risks around data leakage.

Dash solves this by connecting to all of your work apps — from Microsoft, Google, Slack, Notion, everything you use. You get one search box instead of ten. You get AI that actually sees your full picture, not just one ecosystem's slice. And unlike consumer AI, Dash is built for business from the ground up, with security and admin controls that IT teams actually need.

In Q3, we made the product significantly better. Search latency dropped by 75% while quality actually improved. For creative professionals — a core segment for us — Dash now transcribes videos, lets you chat with them, and can search text within images and scans.

We also brought on the Mobius Labs team to push our multimodal capabilities even further. They're building AI models that are optimized for large-scale multimedia processing, opening up entirely new workflows for teams working with video.

And we upgraded Stacks, our intelligent content collections, with ranked answers and simpler sharing. Dash is the only AI tool for SMBs that goes beyond search and chat to actually help organize and share content across your entire company.

We're seeing strong early engagement — 60% of our managed Dash weekly active users are now using Dash at least two days per week, which tells us the product is becoming part of their daily workflow.

And security remains critical. IT admins need to protect their company's content, so this quarter we shipped automated protection for high-risk sharing. Admins can now enforce policies that automatically detect and fix issues like public links or inappropriate external access.

And finally, we made two important announcements during our Fall launch a couple weeks ago:

First, we launched self-serve version of Dash in the U.S. — you can now go to dropbox.com/dash and get your team up and running. No multi-month deployments, no $50k setup fees. Just sign in with your work email, connect your apps, and go. This lets us reach the many SMB customers that enterprise-focused companies can't. We're starting by pricing it at $19 per user per month. And current standard and advanced FSS plan customers are eligible for a 50% first-year discount.

Second, for our Dropbox business customers, we started rolling out native Dash integration inside of the Dropbox app. This brings Dash's search, chat, and Stacks directly into the FSS experience our customers already know. You can ask questions of your files in natural language, get summaries, and find related content. Trial users also get standalone version of Dash for deeper capabilities and the ability to connect to all of the rest of your work apps beyond your files.

Dash within Dropbox is starting to roll out to Dropbox FSS teams on the web, with mobile and desktop coming in the next few months. To ensure a great experience, we're rolling it out in stages over the coming quarters, starting with a waitlist for U.S.-based FSS customers.

This launch represents a significant milestone — they broaden access and introduce Dash to our massive FSS user base and to new SMB customers. Early cohorts are showing good engagement, particularly with search.

We're gathering feedback, improving the product daily, and laying groundwork to convert trials to paid licenses.

Turning to Core FSS, where our focus remains on simplifying and strengthening the user experience while driving efficiency.

We continue to make progress on retention and downsell, driven by better value communication and better optimizing our cancellations flows. And with improved sharing, sync, and storage management tools, our Individuals business just posted our highest-ever CSAT scores.

We're also focused on trial conversion. This quarter we started testing better localization with region-specific value messaging and landing pages, expecting conversion gains over time. We're also testing a low-friction import tool for Google Drive and OneDrive users, making it easier to switch providers right in the signup flow.

Our new unified checkout brings FSS, Dash, and add-ons into a single streamlined purchase flow for Team trials, including an Apple Pay option coming later this quarter. Early results show conversion gains, and we'll extend this to Individual trials later this quarter.

For IT admins, we launched a storage management dashboard showing team data usage and trends — which addresses a top customer request and helps drive our highest-ever IT Admin CSAT score.

DocSend had another solid quarter with double-digit revenue growth, driven by 17% increase in total account creations and strong engagement. The DocSend team is applying learnings from Core FSS to drive retention gains. Sign and FormSwift modestly exceeded expectations.

It's been an eventful quarter. And just like we took the cloud the last mile in 2007 by giving you a folder that synced everywhere, with Dash we're taking AI the last mile by connecting it to your actual work.

With Dash self-serve live and Dash in Dropbox rolling out, we're building awareness, driving trials, and turning early users into advocates. Our Core team is making real progress strengthening and simplifying FSS while operating more efficiently.

The momentum is energizing, and we look forward to updating you on our progress in the coming months. I want to thank everyone on the Dropbox team for all their hard work this quarter.

I'll now turn it over to Tim to cover our Q3 financial performance and Q4 outlook.

TIM REGAN, CHIEF FINANCIAL OFFICER

Thank you, Drew.

I'll cover our financial highlights from Q3, and then provide guidance for the fourth quarter and the full-year 2025.

We executed well against our objectives this quarter, with results coming in ahead of our expectations. Our Core team is making progress stabilizing our self-serve File, sync, and share business areas, while concurrently driving meaningful operating leverage. This is giving us the opportunity to invest in new growth bets such as Dash, which are also making progress as we now have several go-to-market motions up and running to help take advantage of the large market opportunity in front of us. We're also reducing our share count substantially, thus putting ourselves in a position to drive a meaningful increase in free cash flow per share this year.

With this in mind, I'll now turn to our Q3 financial performance.

In Q3, total revenue declined 70 basis points year-over-year to $634 million. Constant currency revenue declined 120 basis points year-over-year to $631 million. Excluding the impact of FormSwift, which acted as a 150 basis point headwind to revenue, our year-over-year constant currency revenue was slightly positive driven by relative strength in our Individuals SKUs.

Total ARR was $2.536 billion, down 1.7% year-over-year, and 1.5% on a constant currency basis. Formswift acted as a 160 basis point headwind to ARR in the quarter.

We exited the quarter with 18.07 million paying users - a sequential decline of approximately 64,000 paying users. The quarter's decline was primarily driven by downsell within our managed account base, as well as our reduced level of investment in Formswift. Counteracting this, we are seeing positive traction from our Simple sku — our lower priced lower storage plan targeted to mobile-first users.

Average revenue per paying user was $139.07 as compared to $138.32 in the prior quarter. ARPU increased sequentially primarily due to FX rate tailwinds as well as shifts to both higher priced and monthly plans.

Non-GAAP disclaimer: Before we continue with further discussion of our P&L, I would like to note that unless otherwise indicated, all income statement figures mentioned are non-GAAP and exclude stock-based compensation, amortization of purchased intangibles, certain acquisition-related expenses, workforce reduction expenses, and net gains on equity investments. Our non-GAAP net income also includes the income tax effect of the aforementioned adjustments.

Gross margin was 81.4% for the quarter, down 260 basis points from the year ago period, reflecting higher depreciation stemming from our data center refresh cycle, as well as investments we are making in our infrastructure for Dash.

Operating margin was 41.1%, ahead of our guidance of 37%, and up roughly 490 basis points from the year ago period. Operating margin increased year-over-year largely due to headcount reductions from our RIF, the elimination of marketing spend for FormSwift, and targeted reductions in Core performance marketing. Compared to our guidance, operating margin benefited primarily from delayed hiring, lower outside services and marketing spend, as well as some one-time benefits.

Net income for the third quarter was $197 million, up 3% year over year. Diluted EPS for the third quarter was $0.74 based on 265 million diluted weighted average shares outstanding, compared to $0.60 in the year ago quarter, representing a 23% year-over-year increase.

Moving on to our cash flow and balance sheet. Cash flow from operations was $302 million, an increase of 10% versus the year ago period. Q3 included $21M of interest payments, net of the associated tax benefit, related to amounts drawn under our term loan facility.

Capital Expenditures were $8 million in the quarter, resulting in unlevered free cash flow of $314 million, or $1.19 per share, up 39% year-over-year. In the quarter, we also added $45 million to our finance leases for data center equipment as we continue to refresh our data centers, though we are nearing the end of this refresh cycle.

As related to capital allocation, in September we amended our existing credit agreement to add $700 million in delayed-draw secured term loans, under similar terms as our initial term loan from December 2024, with no interest expense for undrawn amounts in 2025. We expect to draw these funds early next year to retire our March 2026 convertible notes. As a result, we will not incur incremental interest expense this year related to this transaction.

As of the end of the quarter, we have $1.15B drawn and $1.55B available to draw under our term loans. We ended the quarter with cash and short term investments of $925 million.

Concurrent with our September capital raise, our Board also authorized a new $1.5 billion share repurchase program. In the third quarter, we repurchased approximately 14 million shares, spending approximately $390 million. As of the end of the third quarter, we had approximately $1.58 billion remaining under our existing share repurchase authorization.

I’ll now offer our updated outlook for Q4 and the full year 2025.

For the fourth quarter of 2025, we expect:

Revenue to be in the range of $626 to $629 million. We are expecting a currency tailwind of approximately $3 million. On a constant currency revenue basis, we expect revenue to be in the range of $623 to $626 million. We expect Formswift to serve as a roughly 170 basis point headwind to revenue in the fourth quarter. We expect our non-GAAP operating margin to be approximately 37%. Finally, we expect diluted weighted average shares outstanding to be in the range of 256 to 261 million shares, based on our 30-day trailing average share price.

For the full year 2025:

We are raising the midpoint of our as reported revenue guidance range by $18M, now expecting a range of $2.511 to $2.514 billion. We are also raising the midpoint of our constant currency revenue guidance by $17M, now expecting a range of $2.508 to $2.511 billion. We now expect Formswift to serve as a roughly 130 basis point headwind to revenue this year. Our gross margin outlook is unchanged at approximately 82%. We are raising our outlook for non-GAAP operating margin by 100 basis points to approximately 40%. We expect unlevered Free Cash Flow to be at or above $1.0 billion. We continue to expect cash interest expense, net of tax benefits, of approximately $85 million. We are also lowering our CapEx guidance to be in the range of $20 to $25 million for the full year and we are maintaining our outlook for additions to finance lease lines to be approximately 6% of revenue. Finally, we now expect diluted weighted average shares outstanding to be in the range of 273 to 278 million shares.

Guidance Supplemental Information – FY'2025

I'll now share some additional perspective on this guidance for 2025 and provide some early thinking on 2026.

With respect to revenue, we are raising our full-year revenue guidance to reflect our outperformance this past quarter, as well as stronger structural retention trends across our self-serve skus that we expect to continue through the remainder of the year.

Turning to paying users, we now expect a full-year decline of roughly 250,000, an improvement from our prior outlook of 300,000 paying users. Our better than expected results on paying users is driven by stronger retention with our self-serve FSS skus and the early success of our lower-priced Simple plan. We expect this outperformance to be partially offset by softer results within our managed sales motion, where we continue to see near-term downsell activity. Consistent with our prior commentary, Formswift is expected to account for roughly half of the total decline this year.

Moving on to operating margins, we are raising our full-year guidance by 100 basis points, primarily driven by more disciplined hiring, efficiencies within performance marketing, lower outside services spend, and some one-time benefits. At the same time, we anticipate some incremental investment in headcount and marketing next quarter to support Dash.

We're lowering our full-year CapEx guidance as we've right-sized our data center investments for the rest of the year, consistent with our disciplined approach to managing spend across the business.

We're lowering our full-year weighted-average shares outstanding outlook, reflecting the additional capacity under our share repurchase program and our commitment to reducing share count over time.

And finally, we are raising our unlevered free cash flow guidance roughly in-line with the raise to Operating Margins where we now expect unlevered free cash flow to be at or above $1 billion. Surpassing $1 billion in unlevered free cash flow will mark a milestone for the Company, representing both a level we've been building towards for many years as well as a testimony to the strength of our business model. We're proud of the progress we've made on this front and look forward to continuing the momentum.

FY’2026 Commentary

I’ll wrap up with some early thoughts on 2026. With respect to revenue, our strategy next year will largely reflect a continuation of our goals for this year — with a significant focus on scaling Dash and strengthening our self-serve teams business, all with the aim of returning to revenue growth. However, we expect to continue to face near-term revenue headwinds from our strategic decisions to exit the FormSwift business, as well as to reduce our investments in our managed sales motion and performance marketing for our Core business.

With respect to operating margins, we’ll be lapping the reduction in force we made in October of 2024 and thus will not have this margin expansion tailwind heading into next year. Additionally, 2026 will be an important year for Dash. With expanded go-to-market motions and increased marketing investment, we will aim to drive higher trial usage, engagement, and conversion. As customer traction builds, we’ll retain flexibility to invest further in growth. Consequently, we don’t currently foresee 2026 to be a year of margin expansion.

Having only launched our Dash self-serve motions a few weeks ago, we are just now seeing true customers signals on these motions, and thus will be refining our expectations and plans over the coming months as we gain more insight. Therefore, we will have more to share on our expectations for 2026 during our February earnings call.

With that, Operator, please open the line for questions.