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CLBT.OQ - Q1 2022 Cellebrite DI Ltd Earnings Call

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## CORPORATE PARTICIPANTS

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**Dana Gerner** *Cellebrite DI Ltd. - CFO*

**Yossi Carmil** *Cellebrite DI Ltd. - Founder, CEO & Director*

## CONFERENCE CALL PARTICIPANTS

**Jamie Shelton** *Deutsche Bank AG, Research Division - Research Associate*

**Michael Louie DiPalma** *William Blair & Company L.L.C., Research Division - Analyst*

**Tomer Zilberman**

## PRESENTATION

### Operator

Good day, and thank you for standing by. Welcome to the Cellebrite Q1 '22 Earnings Call. (Operator Instructions) Please be advised that today's conference is being recorded. (Operator Instructions)

I will now like to hand the conference over to your speaker today Anat Earon-Heilborn. Please go ahead.

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### Anat Earon-Heilborn - Cellebrite DI Ltd. - VP of IR

Thank you, Sandra. Welcome to Cellebrite's First Quarter 2022 Financial Results Earnings Call. Joining me today are Yossi Carmil, Cellebrite's CEO; and Dana Gerner, Cellebrite's CFO. This call is being recorded, and a replay of the recording as well as of the presentation that accompanies this call will be made available on our website shortly after the call.

A copy of today's press release and financial statements, including GAAP to non-GAAP reconciliations as well as supplemental and financial information for the first quarter are available on the Investor Relations website at [investors.cellebrite.com](http://investors.cellebrite.com). Statements made during this call that are not statements of historical facts constitute forward-looking statements. All forward-looking statements are subject to risks, uncertainties and other factors that could cause matters expressed or implied by those forward-looking statements not to occur.

They could also cause the actual results to differ materially from historical results and/or from forecasts. Some of these forward-looking statements are discussed under the heading Risk Factors and elsewhere in the company's annual report on Form 20-F filed with the SEC on March 29, 2022, as amended on April 14, 2022. The company does not undertake to update any forward-looking statements to reflect future events or circumstances.

Please note that in the coming weeks, management will participate in a number of investor conferences as detailed in today's press release. Please visit the Events Section of the Investors website to access webcast of our presentations at these conferences where applicable.

With that, I'd like to turn the call over to Yossi Carmil, Cellebrite's CEO.

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### Yossi Carmil - Cellebrite DI Ltd. - Founder, CEO & Director

Thank you, Anat, and thank you all for joining us. I would like to focus in this call on 3 main topics. First, our strong results for the quarter; second, the healthy market environment; and third, the substantial growth potential we have within our existing customer base.

We are excited to report a strong start to the year, delivering strong growth on top of an already robust comparable quarter last year.

We are pleased to report that ARR increased 33% year-on-year and reached \$201 million and revenue increased 17% and reached \$62.4 million. This puts us on track to deliver on our targets for the full year and on our long-term growth objectives. Next, our successful execution was also reflected in a net retention rate of 128% as of the end of March. This is the 13th consecutive quarter with NRR higher than 120%, and we are very pleased with the strength of this metric. And moreover, during the quarter, we booked 18 deals larger than \$0.5 million compared with 17 such deals in Q1 '21, driven by wider adoption of our digital intelligence suite of solutions.

Now, our performance reflects our position as a leading vendor in a growing and healthy market. Our growth is a result of 2 main pillars.

The first is providing law enforcement agencies the broadest, deepest and most innovative digital intelligent suite of solutions on the market. Our solution provides digital evidence collection, review, investigative analytics, investigative management and relevant services, addressing the entire value chain of digital investigations.

The second pillar is our focus on significantly increasing our wallet share within our existing customers.

Now, our go-to-market strategy is designed to leverage Cellebrite's leading market position and strong customer base. Cellebrite has been a driving force in the field of digital collect and review market for many years, and it has always been focused on building a suite of solutions that addresses the needs of hundreds of thousands of investigators, prosecutors and decision-makers in law enforcement agencies.

This digital intelligence suite, which includes collect and review, investigative analytics, digital evidence management, case management and services opens vast opportunities in a very large market, and we believe that we have only scratched the surface of our opportunity in this market. Now given our status as the go-to solution with thousands of law enforcement agencies globally, we believe we are strongly positioned to continue to provide faster, higher effectiveness and more accurate solutions for our broad customer base.

Moving to the second topic on today's agenda, I would like to share our perspective on the market environment. Now over the past few quarters, we have seen a healthy budget environment. This trend continued in the first quarter of 2022, and we expect this to be the case for the rest of 2022. There is a growing pressure on governments to increase police funding to fight crime more effectively and therefore, to deal with the massive growth in digital evidence.

A recent example is President Biden's 2023 proposed budget that includes support for law enforcement, largely at or above 2022 levels.

The willingness to spend in the U.S.A., our main market, reflects an acknowledgment that the fundamental demand drivers for our solutions are continuous. Clearly, the quantity, variety and complexity of digital evidence in investigations are all growing in our world and worldwide customer landscape.

Now in addition, criminals are increasing the use of technology. For example, a few weeks ago, the FBI released its Internet crime report that reveals that the number of Internet crime complaints increased by compounded annual growth rate of 29% over the past 4 years.

Against this backdrop the investigation process must modernize and cannot remain as manual siloed and inefficient as it is. An example that reinforced this necessity is the U.K. Channel 4 News investigation that revealed in late February 2022 that a total of over 21,000 devices, including mobile phones, tablets and computers are waiting to be examined in the U.K. alone.

Now moving to the third topic, let's talk about the substantial growth potential we have within our existing customer base. Now while some customers are more mature than others, essentially all of them are still at the early stages of transforming and modernizing their investigative workflow. Let me now share with you a few examples from the first quarter.

While many agencies continue to focus on adding advanced capabilities at centralized forensic lab sites, a rapidly growing number of forward-thinking agencies are investigating significantly to empower frontline offices in the field. Allowing earlier access to investigative data enables law enforcement to jumpstart investigations. The \$2 million win that we announced in early April with a national police force in EMEA is an example of this type of expansion. The deal reflects one of the largest collection review enterprise deployments to-date, connecting over 100 police stations nationwide.

Another critical growth vector is modernizing the agency's mode of operation through the adoption of high-end investigative analytics and management solutions. In a deal reaching nearly \$3 million, a national police force purchased from us multiple solutions, including investigative analytics to assist with major investigations in a division specializing in organized and drug-related crime. During the proof of concept, investigators achieved quick actionable intelligence for their investigation. Within a matter of hours, they discovered not only what previously took them approximately 6 weeks, but also identified a new person involved in murder case.

And lastly, our domain expertise and scale of operations make our professional services, which we view as an integral part of our digital intelligence suite of solutions, an additional avenue to increase wallet share. In Q1, a large municipal police force engaged with us to help it overcome its digital device backlog through outsourcing advanced collection services at a scope of approximately \$700,000.

Now let's talk about what we do to ensure we continue to realize this massive growth potential and our progress on the plan for 2022 we articulated on our last call.

First, we continue to invest in our go-to-market as planned, in order to develop close and direct relationship with an even larger number of customers.

To that end, we assigned senior account executives to dozens of additional large customers. Now this facilitates higher level of discussions with senior officers that have the mandate to implement digital transformation within the organization.

In addition in Q1, we launched customer councils, which are forums comprising senior decision makers that we intend to convene periodically to exchange ideas on digital intelligence matters. Further, we believe this type of interaction will cement our thought-leadership position in the market.

We continue to invest in our offering in order to expand the suite of solutions and capture an even bigger share of the investigation-related spending.

We highlighted on our last call the need to bring advanced access capabilities to the broader customer base, not just the large law enforcement agencies. As we speak, our team is at Techno Security, one of the leading trade shows in our space, showcasing our premium-as-a-service, our cloud-based collective review solution. This is a flexible licensing option that allows law enforcement agencies of all sizes to access our most cutting-edge technology through a cost-effective cloud-based solution. We are glad to bring our most advanced capabilities to more customers and help them protect and save lives.

And last, we are pleased to announce the collaboration with Chainalysis, which will bring to our customers an integrated block-chain analysis, enriching investigations with information about transactions or networks related to cryptocurrency. Now such partnerships help us ensure that we offer a truly comprehensive digital intelligence suite and bolster our streamlined end-to-end investigative solution, and we intend to continue and pursue additional integration and cooperation opportunities in the future.

So in summary, we are very pleased with the performance in our first quarter of 2022. Our market position is strong and opportunities in front of us are vast. IDC recently validate our position as a market leader in its first ever marketscape for digital forensics. The report is an acknowledgment that the digital forensics discipline as part of the broader digital intelligence market has reached a new level of maturity. And it is a testament for our leadership, cutting-edge technology and domain expertise. It also reflects the crucial and expanding role we play in safeguarding public safety around the world.

And with that, I will turn the call to Dana.

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**Dana Gerner** - *Cellebrite DI Ltd. - CFO*

Thank you, Yossi. As Yossi said, ARR grew 33% year-on-year, reaching \$201 million by the end of March 2022. The main driver for ARR growth is once again the expansion within existing customers, representing 33% year-on-year growth. Yossi gave a few examples on how we sell more

licenses and upsell and cross-sell additional solutions to existing customers. All of these examples fall into this bucket. New logo contributed another 5% growth and in addition, price increases and the transition to term license contributed modestly to ARR growth.

Revenue in Q1 was up 17% from the first quarter last year and reached \$62.4 million. The main growth driver continues to be total subscription revenues that increased 19% year-on-year. Total subscriptions represented 77% of the quarter revenue. Subscription licenses are an important growth driver for Cellebrite as it helps create a long-term incentive to increase customer spending with us. For example, one of our largest deals in the quarter was with a customer that was an early adopter of premium subscription when it was introduced in late 2019. In Q1, the customer renewed its subscription for the third time and extended the length of its commitment.

We also saw strong growth in professional services revenue, which was up 64% compared to Q1 last year, reflecting the resumption of in-person training activity. In most countries, we are back to pre-COVID level of activity.

Our GAAP gross margin was 82.4% in Q1, slightly above our expected range of the full year of 80% to 82%.

Moving to operating expenses, I will discuss this on a non-GAAP basis, so the share-based compensation, amortization of intangible assets, acquisition-related expenses and one-time expenses are all excluded.

Non-GAAP operating expenses of \$49 million in the quarter increased significantly compared to Q1 last year, but only marginally on a sequential basis. It reflects our cost structure as a public company, the increased in-person interaction and related travel and our continued investment in our growth. We ended March with 920 employees, up 17% from the end of March last year. We continue to invest in our cutting-edge solutions and go-to-market efforts and expect to end the year with over 1,000 employees.

Adjusted EBITDA in the quarter was \$4.1 million, reflecting a margin of 7%. This is in line with the typical seasonality of our business. Historically, our revenue in the first half of the year accounted for approximately 45% of the full year revenue. Most of our costs increased moderately throughout the year. This creates a sharper seasonality in profitability than in revenue. We are, therefore, on track to meet our full year margin target of 13% to 15%.

Non-GAAP net income in Q1 was \$1.4 million and non-GAAP fully diluted EPS was \$0.01. Operating cash outflow in the first quarter was \$10.5 million, and in the last 12 months, we generated \$25 million of cash inflow. We ended March with approximately \$172 million of cash, cash equivalents and investments.

We are reiterating our financial year 2022 guidance. We maintain our expectation that December 22 ARR will range between \$250 million and \$265 million, up between 34% and 42% from December 21. We also maintain our expectation for full year '22 revenue to range between \$285 million and \$300 million. We expect Q2 revenue to be higher than Q1 revenue and half 2 revenue to be higher than half 1.

We continue to expect gross margins to be between 80% to 82%. As stated, we are on track to meet our adjusted EBITDA outlook of 13% to 15%, which means \$39 million to \$44 million. Margin is expected to be significantly higher in the second half of the year compared to the first half.

With that, I will turn the call to the operator to open the Q&A session.

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## QUESTIONS AND ANSWERS

### Operator

(Operator Instructions) We have the first question coming from the line of Tal Liani from Bank of America.

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**Tomer Zilberman**

This is Tomer Zilberman on for Tal Liani. Just a quick one for me. NRR of 128% was a bit lower than the past couple of quarters. Just want to get any takeaways there.

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**Dana Gerner** - *Cellebrite DI Ltd. - CFO*

So as we describe when we are transitioning to subscription, we expect ARR and NRR to align throughout the years towards the revenue growth. So this was quite expected, considering the fact that the first step of, moving to subscription provide higher NRR than when you are aligning to a long-term subscription business model.

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**Operator**

Next question comes from the line of Jamie Shelton from Deutsche Bank.

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**Jamie Shelton** - *Deutsche Bank AG, Research Division - Research Associate*

Can you hear me okay?

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**Dana Gerner** - *Cellebrite DI Ltd. - CFO*

Sorry, Jamie, can you repeat?

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**Jamie Shelton** - *Deutsche Bank AG, Research Division - Research Associate*

Can you hear me okay? Just checking.

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**Dana Gerner** - *Cellebrite DI Ltd. - CFO*

Yes, yes, we can hear you.

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**Yossi Carmil** - *Cellebrite DI Ltd. - Founder, CEO & Director*

Quality is not bad.

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**Jamie Shelton** - *Deutsche Bank AG, Research Division - Research Associate*

I was just curious to see how momentum is in getting your UFED base connected to premium enterprise. I think you gave us some helpful color maybe last quarter when it was initially announced. So it was yes, curious to see if there's any momentum there?

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**Dana Gerner** - *Cellebrite DI Ltd. - CFO*

So as Yossi mentioned in the call, we have launched the premium enterprise last year and just showcased the premium as a service. We started introducing customer with premium enterprise, and we are seeing increased number of UFED connected to the premium by having more and more customers adopting the premium enterprise is their main advanced access solution. We do not provide currently exact numbers, but we are on track with our annual expectation and 2022 plan.

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**Yossi Carmil** - *Cellebrite DI Ltd. - Founder, CEO & Director*

Yes just to add that, as we said last time, premium enterprise is our main vehicle to bring advanced capabilities to the field to all UFED obviously, combined with continuous investment on the UFED as such, the access, the decoding and the revenue. So we are basically very pleased with the way premium enterprise is performing at the moment. And as I said, remain the main major growth engine as part of collect and review activity.

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**Operator**

Next question comes from the line of Louie DiPalma from William Blair.

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**Michael Louie DiPalma** - *William Blair & Company L.L.C., Research Division - Analyst*

Given all of the global geopolitical tension, there's been a lot of industry news related to open source intelligence. And with that context, I was wondering, what has been the early adoption for your digital clues acquisition? Has it met your early expectations? And do you have plans for further investing in the digital clues asset and open source intelligence in general?

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**Yossi Carmil** - *Cellebrite DI Ltd. - Founder, CEO & Director*

First of all, I have to say that we are very pleased with the investment and very pleased with the fact that open source intelligence is part of our offering. Q1, we can see that we have an increasing pipeline. I would say, mainly in Europe, Asia Pacific and Latin America. And on top of that, there is a clear strong need in the U.S.A. on the state and local and on the federal side, which is obviously the case.

Good traction on adopting is the investigation space. Again, there are many OSINT tools, but having an OSINT as a standard tool for investigation for policing combined with the digital intelligence or connected to our Pathfinder, this is a key relative advantage of Cellebrite and that resonates very well in police. And there is also expected interest in the intelligence department within the police and in some intelligence organizations. So we are very pleased with the start of the end of promise so far.

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**Dana Gerner** - *Cellebrite DI Ltd. - CFO*

We can also say that we are seeing an increased pipeline.

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**Michael Louie DiPalma** - *William Blair & Company L.L.C., Research Division - Analyst*

Great. And on the last earnings call, I believe you mentioned your target to increase your quota-bearing headcount by 35% this year in order to take advantage of the healthy budget and your pipeline. So I was wondering do you have a status update on that target? Do you still plan to increase headcount by that amount?

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**Dana Gerner** - *Cellebrite DI Ltd. - CFO*

So we -- to my memory, we are speaking about 1,000 plus employees. We are -- we said 920 in by the end of this quarter. And we do expect to cross the 1,000 by the end of the year. This is according to our budget and plans to meet our go-to-market and investment in technology, and we are on track.

**Michael Louie DiPalma** - *William Blair & Company L.L.C., Research Division - Analyst*

Great. And one last one, last year, you announced a partnership with Axon, and you recently disclosed your partnership with Chainalysis. Can you discuss your decision to build the technology yourself versus partnering with a third-party? And how you expect your partnerships with Chainalysis and Axon to evolve over time?

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**Yossi Carmil** - *Cellebrite DI Ltd. - Founder, CEO & Director*

I would say, a generic statement to the partnerships. I think that when a company like us come with a clear aim to build an end-to-end investigative flow from the context of mode of operation of customers, we do not necessarily need to offer everything ourselves. It's a multi-vendor environment, and at the end of the day, we want to bring value to the customer. A key in such a strategy or customer approach is to know how to have an open system and collaborate with other vendors, good vendors, qualitative vendors that together with us, bring value to the customer because that's basically the end of the game. So the go-to-market of Cellebrite is not necessarily doing everything by itself, but also do partnerships, work with channels and obviously, the non-organic part, which is less relevant to what you were asking.

The partnership with Chainalysis is a great value to customers because Chainalysis is a leading blockchain - or has a leading blockchain data platform. And obviously, the usage of cryptocurrency increases, so leveraging on this technology for criminal activity is a key element for our customers. Their expertise will be, I would say, seamlessly integrated into Cellebrite suite of solutions, PA and Pathfinder, and through this partnership, Cellebrite and Chainalysis are offering customers a window, I would say, to sophisticated criminal activity that begin, I would say, funded through cryptocurrency and masked by the anonymity of blockchain. Customers basically are able to identify cryptocurrency-related activities, track the flow, create secure trail of evidence in a single place and part of -- or I would say, as part of the digital investigation.

As for Axon, this is really valuable for the customers, with ability to connect between well-collected investigative data from our tools and analyzed by the Pathfinder and the connectivity, the integration with Evidence.com. So that's in a nutshell regarding the philosophy. That's about those 2: Cainalysis is just starting, Axon - we finished the integration, and we are expecting a mutual approach to customers, again, to bring the value.

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**Operator**

(Operator Instructions) We have no more questions at this time. I would like to hand back over to the speakers for final remarks.

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**Yossi Carmil** - *Cellebrite DI Ltd. - Founder, CEO & Director*

All right. So before we conclude today's call, I would like to thank you all for joining us and wish you all a nice day. Thank you very much.

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**Operator**

That does conclude our conference for today. Thank you for participating. You may all disconnect.

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