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Axon Enterprise, Inc. (AXON)
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MANAGEMENT DISCUSSION SEGMENT

Andrea James *Senior Vice President - Corporate Strategy & Investor Relations, Axon Enterprise, Inc.*

Hello everyone. Thank you for joining us and welcome to our Q2 2022 earnings update. I hope you've all had a chance to read our shareholder letter. We posted that to investor.axon.com after the market closed. And the remarks that we make on today's call are meant to build upon the information that is already in that letter. During this call, we will discuss our business outlook and make forward-looking statements. Any forward-looking statements made today are pursuant to and within the meaning of the safe harbor provision of the Private Securities Litigation Reform Act of 1995. These comments are based on our predictions and expectations as of today, and are not guarantees of future performance. All forward-looking statements are subject to risks and uncertainties that could cause actual results to differ. Materially. These risks are discussed in our SEC filings, and before we go to Rick, we will open with our earnings video.

>>Quarterly Earnings Video<<

Patrick W. Smith *Chief Executive Officer & Founder, Axon Enterprise, Inc.*

Awesome. All right. Well, I will launch in. Andrea and Angel, great job as always on the quarterly video. That's fantastic! Great way to share all the exciting stuff with our shareholders.

We are executing on what is shaping up to be a really excellent year, and our confidence in our growth extends well beyond 2022. We emerged from the pandemic and civil unrest of 2020 in our strongest position ever. And now, we are fortunate to be able to leverage that position of strength while many parts of the economy are experiencing uncertainty.

We are seeing broad-based strength across our product lines. And we are really energized by the growing number of agencies that are buying nearly everything we offer and signing up for 10-year contracts, and sometimes even 12 years.

It's exciting to see an agency go all in with Axon. You know, we set a vision several years ago that an agency wouldn't just say, 'We have a TASER device,' or 'We have Axon body cameras with Evidence.com,' but would instead simply describe Axon as their technology partner, period.

And that's starting to happen now when agencies sign up for all of our software solutions, plus our body camera, our dash camera, the TASER 7, the VR training, our drone solution, and so on.

Customers are increasingly demonstrating their confidence that we are the right technology partner for them, for the next decade. We make it easy for our customers to bet on us, because our team delivers.

On to some other items.

We expect our profitability to improve in the back half of this year— we expect to drive increased leverage coming out of Q2, when we had some expenses that won't repeat. More on that coming from Jim in a moment.

Also, we recently launched an internal campaign, called "spend it like it's yours" — to clamp down on

some low-hanging fruit, such as travel expenses and swag. In fact, we created a new position appointing a swag czar who must approve all purchases. Being scrappy is not new to Axon - we're just taking it to another level of rigor.

I was recently quoted in the Wall Street Journal, it was last week saying, it's, you know, it's good to go on a swag detox, not every event needs a t-shirt and we need to balance the need to travel against what we can do over Zoom, such as maybe setting one or two key representatives to be in the room and having others join online.

We are continuing to hire and invest in this environment — and we are disciplined about it. Our bar for talent continues to move higher. Where we have seen other technology companies slow down their hiring, that presents us with opportunity. And you see some of that in our increased headcount spending in the second quarter. Thinking back to 2008, and that downturn, we invested in creating the cloud and body camera business while our competitors were pulling back. The results of that decision are measured in billions of market cap. Ice Ages favor the adaptable, and we see times like these, when the war for talent cools, as an opportunity to advance our mission so we come out far stronger and more competitive.

Our commitment to generating strong cash flow and operational discipline is shared among the entire leadership team. You'll see in our shareholder letter that we have revised our expected capital expenditures this year to reflect slower pacing on our net campus investments. We are adjusting our pacing to reflect a world that is still in flux as we determine the best and highest use for the campus, optimizing for the new world of hybrid work, as well as the best and highest uses for our capital. It's more important that we get it right than we get it fast, and we are preserving optionality.

Finally, I feel great about the trajectory of our C-suite. Since our last call, Josh Isner was appointed COO and Isaiah Fields, an 11 year veteran of Axon, was promoted to Chief Legal Officer. Also, we have made a lot of progress with our CFO search, which Josh will highlight in more detail. In the meantime, interim CFO Jim Zito hasn't missed a beat.

Before turning the call over to Josh, let me take a moment to share my thoughts about Josh's leadership skills. First, Josh's promotion to COO was really a natural progression for him and for Axon.

Josh has been a rock star since the day he got here and he exudes sheer competence. He built the revenue stream and embodies our core value to "own it." For the past 7+ years, Josh has owned quarterly revenue delivery — where he helped us establish an excellent track record.

Josh is highly focused on delivering results and executing, and exhibits excellent discernment. I'm thrilled with our partnership and our working dynamic — we have a rigorous and healthy back-and-forth and I am very confident in his leadership during this next phase of rapid growth.

And with that, now let me turn it over to Josh Isner.

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

Thanks a lot, Rick. I appreciate that.

Good to see you everyone.

In my new role, I'm humbled by the trust our team, our customers, and our shareholders have placed in me. We are working hard every day to deliver on our mission and drive exciting growth in tandem with

margin expansion.

Here's what that looks like, in terms of where I am investing my time and focus.

First, I am working on building a world class team, from top to bottom. As opposed to focusing on simply filling needs today, I am working with our leadership team to build the team we need for the next 5-10 years. We will focus on a next play mindset, versatility, mental toughness, and capability to deliver outsized outcomes as the core characteristics of our team.

That starts with the search for our new CFO. We have made a lot of progress in this area and we are very excited about the candidates that we have attracted. We hope to have someone to announce shortly that I am personally thrilled about.

And as Rick said, I couldn't be happier about the partnership we've had with Jim. His steady leadership has allowed us to take our time with the search for a permanent CFO. He has been the consummate teammate, and done whatever the team has asked. I sincerely appreciate Jim's leadership.

Second, I will be driving discipline and prioritization across the business. The one thing each of us truly controls is where we focus our attention. We have a lot of exciting opportunities to go after — and as you all know — we will unlock maximal value by focusing our efforts only on the areas where we can have the most impact and deliver the most value for our customers. That is the optimal path for shareholder value creation as well.

For every opportunity we say 'yes' to, we will say 'no' to dozens. And when we do say yes, we will win. From there, our job is to block out the noise and execute.

Third, I will be ensuring that we are aggressively pursuing our total addressable market opportunity. We value that at \$52 billion and it continues to grow as Axon unveils new products and unlocks new markets.

We view our channel as one of Axon's core differentiators, and we will continue to invest into new geographies and customer segments, such as commercial enterprises, Federal and adjacent markets. We will also be scaling our VR, drones, records and dispatch businesses.

For every single one of our product lines — our best days are ahead. That includes the TASER business, which is changing the world for the better and is just getting started internationally. I think you're going to be pleased with what you see unfold here over the next couple of years.

And finally, the entire management team is looking forward to turning on the free cash flow spigot over the next several quarters, which opens up a lot of options for us as a company. This is totally within our control, and we are implementing a plan to optimize the level of execution in this area. We can do a lot better here.

With that, I'll hand the call over to Jim.

Jim Zito, *Interim Chief Financial Officer, Axon Enterprise, Inc.*

Thanks Rick and Josh. Hello everyone, it's great to see you again. We had an excellent quarter, as you can see in our shareholder letter.

Let me put some context around the results and how we are thinking about our outlook ----

Topline momentum continued with growth of over 30% and gross margin improved sequentially. We delivered second quarter Adjusted EBITDA of \$50 million, a margin of about 17-and-a-half percent — largely reflecting some expenses that were unique to this quarter. Let me unpack that for you:

During the second quarter we spent about \$1 million on Axon Accelerate, our annual user conference which has become very strategically important to our sales pipeline, technology leadership and ecosystem expansion.

Additionally, we committed more than \$3 million in incremental mid-year bonuses to employees at the senior director level and below. This was an intentional decision given the team's over-delivery of results in an environment where inflation was impacting their lives.

We did so precisely because we had line of sight to stronger-than-expected revenue both in the quarter and in the back half of the year, which is reflected in our updated outlook. We are especially pleased that we could issue this bonus without affecting our projected Adjusted EBITDA margin percentage for the full year. The fundamental strength of our business allowed us to demonstrate our commitment both to our shareholders and to the team members who work so hard for our customers.

With that context on the quarter, we are already focusing on moderating expense growth going forward to help drive Adjusted EBITDA margin expansion.

Our working capital needs were \$23 million in the quarter — and we have already started to see some of that reverse in July, which is driving us to maintain our full year Adjusted Free Cash Flow outlook.

Finally, I would really like to highlight our commentary in the shareholder letter about our technology partner ecosystem, which was exciting to see in action this past May at Accelerate.

In June, we renewed our strategic technology partnership with Microsoft Azure, who will continue to be the primary host of our software platform and cloud. This is a great partnership for us in many ways. Microsoft is a global leader in cloud technology —of course they need no introduction. Our customers trust Microsoft and thereby feel secure putting their data into our cloud.

As part of the renewal, we extended our contract term for another six years, which gives us long-term pricing certainty and cost visibility for our Axon Cloud business. The renewal supports our software gross margin target of 80%+ and also paves the way for faster international cloud expansion without diluting this target.

And what's also excellent about this partnership is the ability it affords us to offer pricing predictability to our own customers. So, it's just a winning deal all around.

We also highlighted several of our ecosystem partners and strategic investments during our Accelerate conference and in today's letter.

The investments we make are driven by our long-term product strategy, which is set under the leadership of Rick, chief product officer Jeff Kunins and Josh. Our corporate development team, led by

Andrea has been a key thought partner in enabling Axon to grow into its role as the definitive technology hub for public safety.

We take pride in our approach to identifying emerging market leaders in the high value sectors that we know well, integrating their solutions with ours and combining them with the power of our direct sales channel and deep customer relationships.

Importantly, the deal structures our corporate development team have negotiated on behalf of Axon provide us with significant flexibility and optionality on the investments we make. The ability to obtain customer feedback, experiment with product integrations and see how our teams work together allows us to preserve optionality for our business, delight our customers, and expand our technology ecosystem in a highly efficient way.

And with that, Andrea, let's take questions.

QUESTION AND ANSWER SEGMENT

Andrea James *Senior Vice President - Corporate Strategy & Investor Relations, Axon Enterprise, Inc.*

All right, thanks. And here we all are in gallery view. We'll take our first question from Will Power at Baird. Go ahead, Will, you're up.

William Verity Power *Analyst, Robert W. Baird & Co., Inc.*

All right. Great. Thanks, Andrea. Yeah, I propose though too that maybe the next analyst day can be at the racetrack where we can help you test, ALPR. A couple of quick questions, the cloud growth continues to be strong, obviously Evidence.com is a key component of that, but I'd love to hear you unpack any of the other kind of key drivers there. What are you seeing with record management and any of the other kind of key pieces of the software portfolio? What, does attraction and trends look like?

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

Thanks for the question, Will and nice to see you again, I'd say for us, we've talked about this a lot in the video, mentioned our flywheel. For us, the biggest thing we can be doing quarter to quarter is driving the number of officer safety plan subscriptions up. That bundles essentially all our products outside of Dispatch and Fleet, and it provides optionality for customers to opt into records, but it provides a nice base for ARR between the license, all the software add-ons the TASER, the virtual reality, and so for us, that's really the major focus in our state and local business is to drive as many renewals and purchases of that plan as we can. In addition to that, I think we are seeing exciting growth in some of our newer segments. One of which is federal, another is international. And then even in newer ones like Justice and Corrections, we're seeing an uptick. I'd say all of those are combining to just provide a lot of wind at our back as we go on here and we certainly still feel like our best days are in front of us.

William Verity Power *Analyst, Robert W. Baird & Co., Inc.*

That's great. Josh, maybe just one more for you, as you look at the international opportunity in front of you, any perspective on how the macro climate is, or isn't impacting sales cycles, demand trends, et

cetera, that's kind of the broader question. And then number two, tied to international, in your prepared remarks, it sounds like you're feeling better and better about the TASER opportunity, what's driving that optimism?

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

Yeah, absolutely. So internationally in general, to answer your first question, I don't think we're seeing any kind of macro impacts at this point in terms of adoption, interest, buying cycles and so forth. I think we've strongly performed in the TASER segment. We are seeing national police forces buy larger order quantities of TASERs than we've seen in the past, which is really exciting because when we're talking about a national police force, 5, 6, 7 times the size of NYPD and they're starting their purchases in the thousands, the high four digits, into five digit, thousands of units of orders, it's very exciting because we know that we're very good at kind of the land and expand type of playbook. And so we look at these as really good indicators for the future of our TASER business, and we are working with more and more national police forces across the world. And I'd say on top of that, our execution in our tier one markets, the UK, Canada, and Australia has been really strong where we continue to see more adoption of Evidence.com and body cams, but also kind of our newer features on Evidence.com like real-time streaming and transcription, so the next step for us internationally is going to repeat that same level of execution in tier two and tier three markets. And there, you know, we've got to do a really good job of evangelizing the cloud and helping customers understand why the cloud is far, far better as a mechanism for storing and sharing digital evidence. And so we're working through that process. We'll continue to build there, but we're really excited about all the work our international team is doing and they're really focused right now on driving the results upward.

Andrea James *Senior Vice President - Corporate Strategy & Investor Relations, Axon Enterprise, Inc.*

Thank you. Analysts, if you're on this call, we assume you're in queue, so you don't have to keep your hands up. You can, but we've gotcha. We'll take our next question from Erik Suppiger from JMP. Go ahead, Erik.

Erik Suppiger *Analyst, JMP Securities*

Yeah. Thanks for taking the question. Good quarter here. I don't know if you said this, but can we assume that backlog grew from the end of Q1 to the end of Q2 or how should we think about some of the backlog that you carried in from Q4 into Q1 and did that roll into Q2? And then secondly, any comments about supply constraints, did that improve or where are we from a supply constraint, supply chain constraint perspective.

Jim Zito *Interim Chief Financial Officer, Axon Enterprise, Inc.*

I take the first half of that. We disclosed future contracted revenue, Erik, in the letter. So that grew to \$3.3 billion so it was up a little bit less than \$3 billion as of the end of Q2. And then, yeah, there's really nothing, in Q4 we had some unfulfilled demand that that rolled into the first half of the year, but we're sort of back to more normalized levels of sort quarter to quarter. Josh, do you want to take the supply chain piece?

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

Sure thing. And I'd just add that traditionally in the back half, revenue performed stronger than the first half. So, we see plenty of demand still and certainly are going to execute against that demand. In terms of supply chain in general, our supply chain team has been one of our top performing teams at Axon. As

you can see in other businesses, companies are getting hit hard by supply chain constraints. Our team has just done a masterful job navigating through some of those challenges. And frankly, this is one of the reasons we do keep some inventory on the shelves to get through periods like we've had over the last few quarters. And we think at this point, things look better and better each quarter. We do feel that we're through the worst of it and that we'll continue to be able to build the supply orders, but also start to build a little buffer there as well on our TASER and core body camera lines.

Erik Suppiger *Analyst, JMP Securities*

Would you care to guess as to timing when, when supply chain might be relatively normalized, any thoughts where we'll be as we enter 2023?

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

Well, at this point, I don't think we're guessing we're just executing against our plan. And I think by the end of this year, we'll certainly see some buffer in the TASER 7 and AB3 or Axon Body 3 product lines. And from there I think it'll just be about optimizing the level of inventory we keep on the shelves. And from an investor or results perspective, I wouldn't plan on seeing any kind of abnormal activity in either product shipped or inventory backlogs.

Andrea James *Senior Vice President - Corporate Strategy & Investor Relations, Axon Enterprise, Inc.*

All right. Thank you. Next question. Sami Badri from Credit Suisse. Go ahead, Sami.

Sami Badri *Analyst, Credit Suisse Group*

Hi. Thank you. You made a reference earlier, maybe it was Rick, regarding profitability being better in the second half of 2022. And I think you just made a reference that second half revenue growth is, or at least second half revenue production is usually better than the first half. So is there a specific segment or a product that's seeing very good profitable dynamics in the second half, that's kind of giving you guys that operating leverage? That's the first question. The second question is the free cashflow guidance was reiterated and unchanged for the fiscal year 2022, but it looks like there were some changes in CapEx. Could you kind of give us the puts and takes on that?

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

Sure thing. I'll talk briefly about the free cash flow element. Remind me of your first question, Sami.

Sami Badri *Analyst, Credit Suisse Group*

Products that are enabling better profitability in the second half of 2022.

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

Yep. I'll take those two and then I'll kick it over to Rick on the campus piece as well. In general, I think we see stronger bookings in the back half of each year and that's really across all products. Q3 is the end of the fiscal year for several major markets in the U.S. It's also the federal government's end of their fiscal year, so there's a combination of budgets ending and having some money to spend, and then the new budgets starting. If there's a line item for our products, it tends to be a pretty active part of the year. And I'd say the big driver of profitability is the TASER business. And we expect exciting results there, but really across the board, we do see a lot of up-side in the back half of the year.

And in terms of free cash flow, I'd just say we've reiterated our guidance because we feel like, frankly, coming from sales, this to me is not all that different than inside sales. We've got to get in touch with customers, have a process we follow, have well-trained people on the phone, get commitments, follow up on those commitments, and then just get to the point of real predictability there. Jim and I are partnering on that, and we've just brought in a new AR leader. I'm personally investing time with our accounts receivable team to build a playbook where we can really measure efficiency in productivity. But you know, this again, this one is really within our control. And when we couple that, like you mentioned, Sami, with, a better EBITDA, both dollars and margins in the back half of the year, you know, there's a lot of opportunity to improve free cash flow in the back half and we're really focused on it and that's what we're going to do. I'll kick it over to Rick to talk about the new campus.

Patrick W. Smith *Chief Executive Officer & Founder, Axon Enterprise, Inc.*

Yeah, thanks, Josh. So earlier this year we had projected an accelerating spend on the new campus. Now we're basically telling you we're going to slow that down. We're pacing it out a bit. There have been a number of things, I'd say one of them is just the inflationary environment, what we've seen as we were getting ready to really move forward with more of the significant buildout on the campus, construction costs are just up pretty dramatically. And when we couple that with seeing COVID resurging, I think even more than people had expected, and we looked at the whole return to work dynamic, we've come to accept that the future is going to be hybrid work. We also see an opportunity to really look at what is the best use of the overall land, really optimizing for collaborative events, customer-centric events, of course the land that we need and the space we need for manufacturing and warehousing and all that, but maybe shifting the balance away from the idea of people coming into the office so much, and really more the hybrid work environment. And then in this environment as well, like there's a lot going on and we just wanted to preserve some optionality of our cash. We basically said, let's slow down a little bit. Let's really recalibrate and see what the post-COVID world looks like. And let's let the building costs cool off a little bit. And that will give us a little time to just keep tuning and refining. The world is in a pretty constant state of flux, and we'd rather take our time and make sure we get it right.

Andrea James *Senior Vice President - Corporate Strategy & Investor Relations, Axon Enterprise, Inc.*

All right. Next up, Keith Housum at Northcoast. Go ahead, Keith.

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

Hey, Keith, it looks like you're on mute.

Keith Housum *Analyst, Northcoast Research Partners, LLC*

Sorry. You'd think I'd learn, <laugh> thanks guys. Appreciate it. Looking at the TASER gross margins and your commentary regarding improvement in the second half of the year, previously I think the manufacturing automation was going to happen when you're going to build the campus, but it sounds like things are changing. Perhaps touch on what your plans are for a second half of the year and improving the automation and the manufacturing process.

Jim Zito *Interim Chief Financial Officer, Axon Enterprise, Inc.*

Yeah, I would say that's not fully dependent on the campus headquarters. We're already starting to sort of build out that automation. I think part of what we were seeing in the first half was really pressure in terms of growing into our expanded manufacturing footprint. We've been investing to sort of build out

the footprint and capacity to build, and I think as we grow into those build plans, I think we'll see better overhead absorption in there. And I think that's not contingent upon the new building.

Keith Housum *Analyst, Northcoast Research Partners, LLC*

Gotcha. And then the professional services part that the software [inaudible] gross margins, was that in advance of the CAD, the systems you're putting in, or where was that spending being done?

Jim Zito *Interim Chief Financial Officer, Axon Enterprise, Inc.*

I think it covers CAD, RMS, or are sort of the software pieces, but then there's a heavy Fleet portion as well. There's a big uptick in terms of Fleet install. All those things together lead to sort of that PSO revenue becoming a slightly bigger portion of the cloud revenue, but that's sort of enabling sort of that high margin software cloud revenue growth as well. It has set the groundwork for future growth, but I think, you know, PSO is an important part of us controlling that customer experience and really getting sticky customers.

Andrea James *Senior Vice President - Corporate Strategy & Investor Relations, Axon Enterprise, Inc.*

All right. Awesome. Thank you so much. Next question from Jonathan Ho at William Blair. Go ahead, Jonathan.

Jonathan Ho *Analyst, William Blair & Co., LLC*

Hi, good afternoon. I just wanted to understand, first of all, with your head count increases, can you talk a little bit about where you're making those incremental hires and what sort of changed for you to want to make those hires now? I think you referenced a better hiring environment, but curious in terms of your thinking.

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

Yeah, absolutely. I think, look, the last couple years, we've hired very, very aggressively across all segments of the business, and now we're starting in a lot of places to grow into that size and not need to hire as aggressively, but the one major exception to that is in Product. I think from our perspective, we have a lot of great ideas, and we limit those based on where we think we have the most upside and also the size of our team and what our team can take on. And so as long as there's talented engineers, product managers on the market that can help us deliver product faster and build products that we feel can really change outcomes in public safety, we're going keep investing there. I think going into next year, the mindset is going to be get a little leaner in terms of our hiring plans and SG&A, and continue to be aggressive where we can on in R&D.

Jonathan Ho *Analyst, William Blair & Co., LLC*

Got it. And then just as a follow up, when we think about some of the cost savings initiatives that you referenced either on the T&E side or other areas, can you talk a little bit about maybe philosophically where you're seeing that opportunity, "spend it as if it's your own," I know I'm not saying that right, but that campaign, I just want to understand, do you feel like there was maybe lack of oversight there in the past, or is this a situation where you're just trying to tighten the belt a little bit? Thank you.

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

I'm not sure it's a lack of oversight. I think certainly we've got very good controls and process in place to measure expenses, but I think at times we've gotten just a little bit bloated in how we think about things from the number of people that attend meetings with customers, like Rick mentioned, or swag is another obvious one where we have maybe due to the absence of being in the office, we've used swag as a way to kind of connect with our employees. I think there are opportunities to get a little more efficient in those places. It's not necessarily an indictment of anyone or anything we've done in the past. It's just more like the landscape changed a little bit. We see all this exciting revenue growth well into the future and it's just a matter of getting leverage out of that growth where we can without impacting our employees' sentiment at Axon. And I think we can thread that needle very effectively.

Patrick W. Smith *Chief Executive Officer & Founder, Axon Enterprise, Inc.*

Yeah. Let me, let me jump in and add as well. A business, like any community, can't have all messages, all resonate all at the same time, so you go through cycles. Several years ago, we had a "Be Scrappy" year where that was an opportunity for us to lean in. It's very similar to what we're doing now with "spend it like it's yours," right? The whole "Be scrappy" was to focus on finding ways to more efficiently get things done and reward people for being scrappy and not throwing a body at every problem. We've had a fair number of new employees come in and certainly we have our standard expense controls and training, but we felt with what's happening, the overall market is down, inflation is up and other companies are I'd say more aggressively cutting back their investment plans, we saw this as an opportunity to communicate with our employees like, "hey, spend it like it's yours," right? This is a moment. Let's consider what is going on outside. Everyone has things in their control where they can cut back spending, and by doing that, we'll all be rewarded. The market is rewarding companies that have more financial rigor, and we can also reward you by investing and not having to pull back on our investment plans and the exciting things we want to go build. We can't just be tone-deaf and continue as if the macro environment hasn't shifted. I think this was a balanced way for us to connect with, maybe even relieve some of the angst our employees may be feeling about the macro environment by saying, "hey, here's something you can do, really buckle down on expenses so we can continue to invest over here," because we know these are the times those investments really pay off. Our hiring has accelerated. I think a big part of that is it's the macro environment. We don't have as many competitors. We're having more success recruiting because we're just not competing with as many other tech companies that are as aggressive right now. These are the times we want to lean in and accelerate our growth. So, I hope that gives a little bit of context as to how we felt we could position this with the company employees to really get them all rowing in the same direction.

Jim Zito *Interim Chief Financial Officer, Axon Enterprise, Inc.*

The only fact I'll add to that is overall travel costs went up at the same time as we dealt with that pent-up, post pandemic demand. And as Rick said, as we adjust to the best way to operate in the most efficient ways, from a travel and hybrid perspective going forward, I think we'll thread the needle a little bit better in terms of meeting that. And I think everybody's plays are focused on that.

Andrea James *Senior Vice President - Corporate Strategy & Investor Relations, Axon Enterprise, Inc.*

All right, awesome. Josh Reilly at Needham. You're up next.

Josh Reilly *Analyst, Needham & Co., LLC*

All right. Thanks Andrea, for the questions. TASER revenues obviously were very strong in the quarter, quite a bit above what we were modeling. You touched on this a bit, but how much of the back orders you expected at the end of last year to be complete, I think you had mentioned previously by the first half or now through, I think you mentioned it was like \$30 million? And then can you remind us if there's any seasonality to TASER shipments and if that could affect Q3 or Q4 TASER revenue, just so we have an idea sequentially?

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

Yeah, absolutely, Josh, thanks for the question. I'd say it's fair to say we're caught up on the TASER shipments from Q4 last year and we've shipped those over Q1 and Q2 and because sequentially TASER shipments go up in the back half of the year, we still feel like Q3 and Q4 will be the highlights of the year revenue-wise. And so, I think that's kind of the story. Q4 tends to be a little higher than Q3, but you know, over the years we've seen the inverse of that as well. But as a back half, we certainly have a lot of confidence that we'll outpace the first half of this year in revenue.

Josh Reilly *Analyst, Needham & Co., LLC*

Got it. That's super helpful. And then on the Axon Fleet units, those increase nicely as well, quarter over quarter. Should we assume that all of those are Fleet 3 at this point, or are you still shipping any Fleet 2? And then how should we think about the level of supply constraint versus demand for that product?

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

In terms of the mix of Fleet, there's still a little bit of Fleet 2, but mainly Fleet 3. And of course, a lot of body camera shipments going out. Supply chain constraints, I'd say we have plenty of supply to deliver on our guidance in the back half of the year, product by product. When we get outside of the core TASER and body camera products, there's a little bit of flux month to month there, but in a macro sense we are feeling great about where we stand from an inventory perspective.

Andrea James *Senior Vice President - Corporate Strategy & Investor Relations, Axon Enterprise, Inc.*

All right. Jeremy Hamblin from Craig-Hallum. Go ahead, Jeremy.

Jeremy Hamblin *Analyst, Craig-Hallum Capital Group, LLC*

Thanks for taking the questions. Congrats on of the strong momentum in the business. So federal contracts, clearly a pretty key segment right now, really a big driver of the business, ton of momentum there, I wanted to get a sense for whereas we've seen an executive order mandating federal agencies to use body cams, wanted to get a sense for what you're seeing internationally in terms of that type of mandate, that type of adoption. Typically, there's been a decent lag period between instituting that type of policy, but there have been significant incidents both in English speaking world as well as other places with surprises and incidents, Japan comes to mind, where we wanted to get a sense for what the pulse is of other government agencies around the globe.

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

Yeah, I think it's a good question, Jeremy. As you'd expect, it varies a little bit. I'd say just like the United States, Canada, Australia, and the UK were relatively early adopters of body cams. So, even if a mandate were to come down at this point, I don't know that it would change the buying behavior all that much in those three markets. I think the market has decidedly already shifted to body cameras there. In other markets we're starting to see international governments are starting to dip their toe a little bit into the body camera world and start to understand kind of what's going to work for them and what's not. And I think we do have a lot of opportunity there first with kind of small and mid-size orders and then growth over time. And so that's really where we see kind of international going in terms of body cameras. But like I mentioned, we are seeing international governments start to deploy TASERs with a lot more conviction around the globe and we should expect to see that continue for the years to come.

Jeremy Hamblin *Analyst, Craig-Hallum Capital Group, LLC*

As a follow up question, domestically federal contracts, in terms of the value that you're getting in those deals, right, you're talking about a huge buyer, a buyer that's been mindful, to look at getting best pricing, et cetera. So wanted to understand in terms of length of contracts there and any kind of the value you're getting the ASPs, how that compares obviously without getting into, exact specifics, but just understanding that a little bit in terms of that buyer?

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

And is that for international specifically?

Jeremy Hamblin *Analyst, Craig-Hallum Capital Group, LLC*

No, domestically.

Patrick W. Smith *Chief Executive Officer & Founder, Axon Enterprise, Inc.*

I think the question was about our federal buyers.

Jeremy Hamblin *Analyst, Craig-Hallum Capital Group, LLC*

Federal, correct.

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

Federal government is generally mirroring what our state and local customers are doing pricing-wise. Certainly, we do have some commitments to make sure that we are recognizing the federal government and the most-favored nations clauses in some of those contracts, but ultimately, we do feel pretty good that those license types and sizing is similar to what we see and far, far, far ahead of when our state and local customers started to buy. And in large volumes, like the federal government has kind of skipped that phase of basic licenses and tap, and they're buying a lot more frequently at higher license types, which is exciting.

Patrick W. Smith *Chief Executive Officer & Founder, Axon Enterprise, Inc.*

Yeah. And I would add Josh as well that we're starting to now invest in dedicated federal R&D. So, in many cases we're seeing the fed customers interested in premium features that might even require a little more investment in certain terms of hardening of different devices or software to meet certain federal requirements that in some cases can even lead to premium pricing.

Andrea James *Senior Vice President - Corporate Strategy & Investor Relations, Axon Enterprise, Inc.*

All right, we have one more analyst and then if any of you guys have a follow-up, we'd love to take your follow-up because it looks like we will have time. We'll take our last question from Erik Lapinski at Morgan Stanley. Go ahead, Erik.

Erik Lapinski *Analyst, Morgan Stanley & Co., LLC*

Thank you. I just maybe wanted to follow up on the federal market and some of the comments you guys just made there. I'm curious in terms of bundling that you're seeing in the federal market, are you seeing similar uptake of OSP 7 +, I know that a number of agencies already have TASERs, so are they looking at body camera contracts kind of separately or up bundling when you see those deals? I'd be curious on kind of what it looks like.

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

Yeah, great question, Erik, I'd say we're seeing department by department, a little bit of everything. I think the agencies, you mentioned that agencies already have TASERs, a lot of those are up for upgrades, so it's a great time to buy our body cameras and software and bundle that upgraded version of the TASER in with that contract. Other customers are buying software only, our investigator package for certain customers in the federal government, and, then some standalone activity as well. There's a lot of really encouraging things here, but one of them that stands out is customers are also buying across our suite of products. They're seeing use cases for live streaming. They're seeing use cases for Records. They're seeing Fleet 3 interest, and so really across the board, we're seeing a lot of interest in a lot of different products from the federal government and it's really a credit to the work Richard Coleman, our head of Federal and his team have done. It's really transformed over the last few years from a steady state market into an exponentially growing one.

Erik Lapinski *Analyst, Morgan Stanley & Co., LLC*

Thank you. That's helpful. And if I could sneak in another one, I know the corrections market is kind of another expansion area for you guys that we didn't talk that much about this quarter. I'd be curious if just any, whether it's from funding initiatives you're tracking or just what the states are looking at in terms of the corrections market, if you're seeing more of an uptake there? I know there had been a couple early prisons over the past couple of quarters, but just in terms of kind of building on top of that.

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

Yeah. The team is definitely growing and for us. I think it's less about the federal government giving grants or fundings or any kind of overall market effects there. I think it's more just historically we hadn't really had a team focused on corrections as its own market. We really did a lot of correction sales through the Sheriffs' office while they were buying products for the rest of their deputies. And now just having a really focused team, we're starting to unlock a lot of that market on a much more predictable basis. I think the growth there is just attributable to our team's focus as opposed to any external factors.

Andrea James *Senior Vice President - Corporate Strategy & Investor Relations, Axon Enterprise, Inc.*

Great. Looks like we have a follow up from Jonathan Ho at William Blair. Thanks Jonathan.

Jonathan Ho *Analyst, William Blair & Co., LLC*

Yeah, just a couple from me. I wanted to maybe dig a little bit into your Microsoft opportunity. Can you talk a little bit about the level of benefit or cost savings that you could maybe see from that deal? Just as a starting point.

Patrick W. Smith *Chief Executive Officer & Founder, Axon Enterprise, Inc.*

Yeah. I'd start by saying the exact terms of the deal are not something we can go public with.

Jim Zito *Interim Chief Financial Officer, Axon Enterprise, Inc.*

I'd say at high level, it supports our target long term of having 80% + software gross margins. And I think the duration of that contract is really helpful for us for having that confidence and visibility to our pricing when we set our contracts with customers. I think it helps us over time to maintain/ expand our Axon cloud gross margins, but I think the best thing that it does is gives us predictability.

Jonathan Ho *Analyst, William Blair & Co., LLC*

Got it, got it. And then, just in terms of the commercial market, can you talk a little bit about your progress there and maybe some of the go to market opportunities that you see specific to commercial? Thanks

Joshua Isner *Chief Operating Officer, Axon Enterprise, Inc.*

Yeah, we're thrilled with the opportunity there. Mike Shore and his team have just done a great job building something. We don't get those same advantages we sometimes have in the public sector with the referral network and stuff. We have to build those from scratch and Mike and his team have done a great job of that. The team continues to be on a cadence of doubling every year and that's happened in terms of their results for the last three years now. We're still probably about 90% of the way there on product market fit, where we've got some really evangelical early adopters that are excited about how things are going. Now it's just kind of closing that last 10% of some of the product market fit items and really expanding each year.

And I think we're really, really well positioned to do that. And you'll start to see some names that you're very familiar with adopting our products for more commercial purposes.

Andrea James *Senior Vice President - Corporate Strategy & Investor Relations, Axon Enterprise, Inc.*

All right. Do we have any other follow ups? We'll give you a second. I can see you guys thinking. Okay. All right. Let's have Rick close us out.

Patrick W. Smith *Chief Executive Officer & Founder, Axon Enterprise, Inc.*

All right. Well, obviously another great quarter. I'm really proud of what the team was able to deliver. There's a lot going on in the world and our team just really digs in and Josh just does a great job of keeping people focused, blocking out the noise. There's a lot happening in the world that we can't affect, but there are things within our control and the more we focus, the better the results always end up being. So, I appreciate everybody joining us today. And we look forward to updating you on the back half. Have a great day.

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