



ShotSpotter, Inc.

Second Quarter 2018 Earnings Call

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CORPORATE PARTICIPANTS

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Jaeson Schmidt, *Lake Street Capital Markets*

Jeremy Hamblin, *Dougherty & Company*

Joseph Osha, *JMP Securities*

Robert Stone, *Cowen and Company*

PRESENTATION

Operator:

Good afternoon, and welcome to ShotSpotter's Second Quarter 2018 Earnings Conference Call. My name is Steve (phon), and I'll be your Operator for today's call. Joining us are ShotSpotter's CEO, Ralph Clark; and CFO, Alan Stewart.

Please note that certain information discussed on the call today will include forward-looking statements about future events and ShotSpotter's business strategy and future financial and operating performance. These forward-looking statements are only predictions and are subject to risks, uncertainties and assumptions that are difficult to predict and may cause the actual results to differ materially from those stated or implied by those statements. Certain of these risks and assumptions are discussed in ShotSpotter's SEC filings, including its registration statement on Form S-1. These forward-looking statements reflect Management's beliefs, estimates and predictions as of the date of this live broadcast, August 2, 2018. ShotSpotter takes—undertakes no obligation to revise or update any forward-looking statements to reflect events or circumstances after the date of this call.

Finally, I'd like to remind everyone that this call will be recorded and made available for replay via a link available on the Investor Relations section of the Company's website at ir.shotspotter.com.

Now I'd like to turn the call over to ShotSpotter CEO, Ralph Clark. Sir, please proceed.

Ralph Clark:

Good afternoon, and thank you to everyone joining us today. Alan and I look forward to taking your questions after we provide a review of our Q2 performance.

In a nutshell, it was another solid quarter for ShotSpotter, with continued strong financial execution and implementation of a variety of operational initiatives that we believe keep the Company well positioned for continued growth in this large and untapped market space.

Based on our near-term visibility and positive momentum, we're tightening our revenue guidance for the full year of 2018 from \$33 million to \$34 million to \$33.5 million to \$34 million. The midpoint of the new full year guidance reflects an anticipated increase of 42% from 2017.

Q2 revenue was \$8.9 million, an increase of 53% from a year ago and 29% sequentially from Q1. Gross margin expanded to 56%, and we managed to come close to achieving breakeven with a net loss of only \$369,000. This amount included expenses related to the write-off of three deployed indoor sensor installations. We see a larger opportunity in outdoor and have made the strategic decision to no longer include indoor coverage as a part of our service offering. However, we were recently awarded a patent on our indoor sensor technology, and we're evaluating the most effective way to leverage that IP, which may include partnering with established indoor players to operate combined solutions where there is demand.

Alan will provide the financial detail, but I want to stress how encouraged we are to be driving top line growth with expanding gross margin while tightly managing our operating cost structure. We're ahead of schedule here, and we're confident about our ability to cross over to GAAP profitability later this year. That confidence is a reflection of our growing sales pipeline, accelerated new bookings and projected go-live miles of ShotSpotter with new and existing customers.

This quarter, we went live on 61 new miles without a single mile of attrition. Those miles were comprised of existing city expansions, two new city deployments in Baltimore and Calumet City and our eighth SecureCampus deployment at Hampton University. Since we have a fair number of new folks on the call who are still getting acquainted with our business model, I do want to stress that while we had a great Q2 with respect to go-live miles, our internal focus remains on annual new miles deployed. Adding new go-live miles can often be lumpy quarter-to-quarter due to the administrative bureaucracy of contract execution and the time invested in getting sensor placement permissions as a part of our deployment process. This varies from client to client and can sometimes make quarterly comparisons less than meaningful.

On our last call, I talked a bit about our growing focus on the international opportunity, including the addition of our new VP for International Sales for Latin America, Jon Magin. Jon is already making solid progress, having visited for five countries in the region and having met with several police agencies, local integrators and solution partners. We believe that interest is high and the need is significant, and we remain confident that the ShotSpotter solution can help mitigate the large problem of gun violence in Latin America.

We're also targeting other international areas of opportunity. I recently got back from a productive trip I South Africa, where I met with multiple municipalities and provincial government representatives as well as with key legislators at the national level, many of whom were already familiar with ShotSpotter from our successful Cape Town deployment. In fact, while I was in country, there was a significant amount of media coverage on the conviction of a well-known Cape Town gang member that was based on a ShotSpotter alert, combined with video surveillance.

I also got out to Kruger National Park, where we've been expanding to an operationalized coverage area of ShotSpotter that is helping combat rhino poaching. This is an exciting project, as it allows us to test our capabilities in a harsh environment at operational scale. Our objective is to attract philanthropic support to further expand and continue protecting the world's few remaining rhinos. That's a quick look at our last three months.

I think it's worth noting that Q2 pretty much continues the progress that we have steadily been making since going public a year ago. For those of you on our IPO roadshow, you'll remember that our plan for growth was to focus on leveraging our strong market position and commitment to positive, long-term client relationships. As many of you know, the ShotSpotter deployment typically starts with just a few square miles. Then we collectively prove how powerful the impact can be at responding to gunfire incidents and building goodwill and confidence from citizenry in those communities. Customers then seek to expand the solution to help police redouble their effectiveness.

To date, approximately 40% of our Flex customers have expanded their initial ShotSpotter footprint. Our growth plan was to also steadily add new jurisdictions to our customer base. We've done that as well by adding 12 new key cities in 12 months since our IPO, including Baltimore, Atlanta and Las Vegas, to name a few.

We also indicated on the road show how important international markets could be and how large the opportunity is overseas. International sales cycles can be lengthy, so we're happy that Jon is already gaining traction, and we are cautiously optimistic about adding new international customers next year.

We also acknowledge that our sales growth was not going to be driven purely by our internal efforts. We know how large this opportunity is, and we know that in order to succeed, we're going to need more routes to market. To that end, we have focused on building strong relationships with GE Current, AT&T and Verizon in getting ShotSpotter more deeply ingrained in their Smart City initiatives.

Finally, and most importantly, we continue to believe that delighted customers are the best evangelists for ShotSpotter. Indeed, we see them as another key sales channel. The resources we've added to ensure customer success have led to high revenue retention rates and strong customer advocacy, represented by our NPS score of 55. We cannot overstate how important it is to our continued growth to have a Chief of Police share with one of his or her peers in another agency how valuable and effective ShotSpotter has been in mitigating their community gun violence problem.

In summary, we've had a plan for growth and we've stuck to it. Our success has not been an accident. It is also not anywhere near complete. We're serving a large and largely untapped market, and the key is continuing to successfully execute against the opportunity. It's still the early part of our story, and we think the best and most exciting part of that story is still ahead of us.

Okay, that covers my prepared remarks. I look forward to your questions. But first, here's Alan to review our Q2 results in more depth.

Alan Stewart:

Thank you, Ralph, and good afternoon, everyone. We're encouraged to report another quarter of record revenue, again exceeding expectations. Revenue was \$8.9 million, up 53% from \$5.8 million in Q2 of last year, with 61 net new miles deployed in the quarter. We're extremely excited to be so close to our goal of achieving GAAP profitability.

In Q2, we realized a net loss of \$0.03 per share. As Ralph mentioned, had we not had the write-off related to indoor sensor deployments, we would have been extremely close to breakeven. We're therefore reaffirming our target of achieving our first quarter of GAAP profitability by Q4 2018. In addition,

our solid execution and strong second quarter is allowing us to again tighten our full year revenue guidance.

Let's look at the details of the quarter. As I mentioned, revenue for Q2 was \$8.9 million, an increase of 53% over second quarter of 2017, the sixth consecutive quarter that our revenue exceeded our long-term growth target of 35%. Revenue was driven by growth in the number of miles covered through expanded deployments for current customers and the addition of new customers.

Also included in Q2 revenue was some catch-up revenue from contract renewals due in Q1, as well as a bit of NRE from our technology integration with Verizon.

Gross profit for the quarter was \$5 million or 56% of total revenue, up from 54% in second quarter 2017. We were particularly pleased with the gross margin, as it was negatively impacted by charges related to the write-off of the three indoor sensor deployments. Without these expenses, gross margin would have been approximately 4 percentage points higher. We're still evaluating the disposition of the remaining indoor sensor inventory. That said, we still expect gross margins in Q3 to be slightly higher than Q2.

As a reminder, last quarter, we introduced Adjusted EBITDA as another metric by which we measure our operating results. In Q2 of '18, Adjusted EBITDA, which is calculated by taking our GAAP net income and adding back net interest, taxes, depreciation and amortization and stock-based compensation was \$1.2 million. We expect Adjusted EBITDA to remain positive in all future quarters.

Operating expenses for the quarter were \$5.3 million, a 61% increase over the prior year period. Our operating expenses are increasing as we add to our staff in all expense categories.

Sales and marketing expense for the quarter were \$2.2 million or 25% of revenue versus \$1.4 million or 24% of revenue in the prior year period. As we have discussed, this increase reflects our continued expansion and the related expenses of our domestic and international sales and marketing efforts.

R&D expenses for the quarter were \$1.3 million or 14% of revenue compared to \$928,000 or 16% of revenue in the prior year period. We continue to invest in R&D to expand the applications for our technology, improve our analytics capabilities and conduct other initiatives.

G&A expenses for the quarter were \$1.8 million or 20% of revenues, which is an increase from \$971,000 or 17% of revenue for the prior year period. For the second half of the year, we expect operating expenses to increase marginally on a dollar basis in all categories as we continue to add to our headcount.

The second quarter GAAP net loss was \$370,000 or \$0.03 per share compared to a loss of \$4.3 million or \$1.16 per share the prior year period. We deployed 61 net new miles in Q2, up from the 44 miles deployed in Q2 of 2017. While we're extremely pleased with the strength of the quarter, as always, we remind you that deployments can be lumpy so the quarterly go-live miles will vary by quarter.

Deferred revenue quarter-end was \$17.4 million, of which \$16.2 million was short term and \$1.2 million was long term. In general, we expect short-term deferred revenues to be recognized within four quarters. Again, we caution you should not read too much on the quarterly changes in deferred revenue as timing during the quarter of when new miles go live can have a significant impact on deferred revenue. We consider this another metric that is more informative on a year-over-year basis versus quarterly.

We generated cash from operations for the quarter of \$1.4 million. We ended in a solid financial position with \$14.8 million in cash, up slightly from first quarter, and we have no long-term debt.

Due to the strength of our second quarter results, we are tightening our guidance for the full year 2018. We remind our investors that our third quarter revenues are typically flat from second quarter due to contract renewal cycle.

For the full year, we now expect revenues of \$33.5 million to \$34 million, the mid-point of which is up slightly from the \$33 million to \$34 million guidance we provided last quarter.

Our confidence in our full year outlook is based upon the strength of our deferred revenue, our historically strong renewal rates and new contract awards scheduled to go live.

As Ralph noted, we are very encouraged by our progress since the IPO last year. The visibility in our business model has allowed us to achieve our plan, driven by the solid execution and commitment of the ShotSpotter team. We look to continue this trend for the balance of 2018 and in the years ahead. We look forward to sharing our progress with the you as we help police departments around the country and eventually around the world reduce gun violence, increase officer safety and improve community relations.

Now, we will be happy to answer your questions. Thank you.

Operator:

We will now begin the question-and-answer session. To join the question queue, you may press star, then one on your telephone keypad. You will hear a tone acknowledging your request. If you are using a speakerphone, please pick up your handset before pressing any keys. To withdraw your question, please press star, then two. We will pause for a moment as callers join the queue.

Now, our first question will come from Richard Baldry with Roth Capital.

Richard Baldry:

Thanks, and congrats on a great quarter. When I look at the mid-point in guidance and I back out your first half, it would imply essentially flat revenues for the next two quarters. That's out of pattern with the trend we've seen, so could you maybe talk about the magnitude of catch-up revenues in the quarter and NRE, nonrecurring engineering revenues, in the quarter, so we sort of get a feel for how much that's changing the seasonality versus years before? Maybe comparative to maybe just how conservative we think you're being for the second half guidance?

Alan Stewart:

Sure. Thanks, Rich. This is Alan. There was about \$0.5 million in Q2 that was related to catch-up revenue and some NRE. I think if you would normalize that, you take that out of that, it would probably normalize close to around 8.4.

Richard Baldry:

Okay. On the 61 net new miles that's, I think, the highest number that we've seen. Was that balanced sort of across the country? Are there some areas that you think are moving faster? How much do you feel like that's a sustainable level on sort of an annualized level versus maybe just a really good quarter and a bit of a standout?

Ralph Clark:

Yes. This is Ralph. Thanks for that question, Rich. I think it's fair to say that our Q2 go-live number was an exceptional one. What we've tried to do is make sure that people understand that you can't take out a

single look at a single quarter, I would say, and then make general assumptions about what we could drive in future quarters. We tend to look at this on an annualized basis. That being said, I think we've got a great project manager team and installation crew. We have a pretty strong bookings backlog that we're still adding new miles on. We're going to be lighting up miles certainly in Q3 into Q4.

Richard Baldry:

I know you don't like to talk about clients until they're further down the path, but seeing a city like Toronto which most people think of as fairly safe, have an incident and then quickly have their city council pass funding for ShotSpotter implementation is a little bit out of the norm. Can you maybe talk about how much broader you think the market could address sort of non-typically less violent areas with sort of Toronto as a guidepost? I don't think people would have thought that, that would be a typical customer opportunity.

Ralph Clark:

Sure. I think we've always said that it's really difficult to look at violent crime across an entire city. There's a number of cities that, in aggregate, look quite safe. But when you look at three to four or maybe five square miles of any city, and I'll just pick Seattle would be another example of one, where that three- to five-mile square area could look very much like a more high crime area that you'd expect to see in a place like maybe Baltimore, Philadelphia or Chicago and the like. I think it's a little bit of a misnomer to kind of think of cities being generally safe. Because everything city, or not every city but there's a number of cities that do have these problematic areas that are at-risk neighborhoods that are suffering from gun violence, and Toronto is no different than that or any other city in that regard.

Richard Baldry:

Great. Congrats, again.

Ralph Clark:

Thanks, Rick.

Operator:

Your next question is from Tim Klasell of Northland Securities. Please proceed.

Timothy Klasell:

Hey, guys. Congrats on the nice quarter. A question, sort of a follow-on to the prior questions. What are you seeing with your sales cycle? I think you mentioned the word-of-mouth amongst the police chiefs and what have you. Are you beginning to see sales cycles shrink or maybe more of a pull action than a push action?

Ralph Clark:

Yes. Great question. We're seeing certainly a lot more chatter, and I think as we said in our prepared remarks, the value of having strong advocacy of chiefs that are using the service and driving great outcomes is certainly helping accelerate our sales cycles. That being said though, this is still a complex sales cycle, and I don't think we should expect sales cycles to collapse to anything, any period less than 12 months. I think that the model that kind of we're looking at is really a 12- to 18-month sales cycle, which is a pretty big improvement over where we say two to three years ago, where the sales cycles could be more like two years.

Timothy Klasell:

Okay, great, great. Then, I think in the call, you were mentioning that you would hope to see something in the international by next year, which sort of reinforces what you just mentioned about the sales cycle. But as you look at those geographies and the conversations that you're having, is there any stand-out differences in those contracts as far as the size, the pricing or anything else that investors should be aware of?

Ralph Clark:

I think we talked probably about the fact that we have a little bit more pricing leverage internationally, so the price points are higher. In the case of South Africa, Cape Town, I think our price is something like \$100,000 per square kilometer per year. We know we're probably going to have to come off of that a little bit, especially when we enter into longer-term contracts. The reason—one of the reasons that we can charge more in those international markets is the cost is a little bit more, but also we're tending to deal with more federalized police departments. They're a little bit more well-resourced and perhaps even you can say a little bit more sophisticated in terms of kind of taking on very large projects. That enables us to price a little bit higher than what we do domestically.

Timothy Klasell:

Okay, great. Then one final one. The sales force headcount, I know you added a little bit this time last year. Any plans in the near term that we should be aware of? Where would you like to expand? Thanks.

Ralph Clark:

Yes. We're continuing to invest in our customers' success and onboarding organization there. That's a complement to the direct field sales force. We feel that, that's the best bang for our buck, if you will, because again, kind of creating very strong advocates within the customer installed base is critical to our growth, and there's a number of examples that we can point to where a very satisfied chief has had a conversation with another chief, has gotten them to consider ShotSpotter. We'll continue to invest in that onboarding customer success organization. It helps protect our renewal rates, but then it also helps accelerate sales. Then we have enough sales, direct sales people, to go kind of execute those deals, kind of once they bubble up to the top.

Timothy Klasell:

Okay, great. Thank you very much.

Operator:

The next question is from Saliq Khan with Imperial Capital. Please proceed.

Saliq Khan:

Great. Thank you. Hi, Ralph. Hi, Alan.

Ralph Clark:

Hi, Saliq.

Saliq Khan:

Just a couple of questions from my end. The first one being is, with the gross margins being improved and being well above what my estimates were, should we continue to expect the gross margins to keep

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up the trajectory for the remainder of the year? Or should I expect it to be tapered back the back half of the year?

Alan Stewart:

Saliq, great question. This is Alan. In Q2, a larger portion of focus was actually on customer deployment as opposed to sensor maintenance. With 61 go-live miles, there are a lot more deployments. When we do the deployments, that actually adds more costs that get combined and depreciate over five years as opposed to straight sensor maintenance costs which are expensed during the period. Although I would say it would fluctuate a bit, we are ahead on our gross margin percentages. I think, as I mentioned in the call, we do expect Q3 to be even slightly higher than Q2 was.

Saliq Khan:

Perfect. Then, you guys have done a recent S-3 filing for a \$50 million shelf offering. Today, you had talked about the Company's intention to no longer be in the Eagle solution business. How should I be thinking about the best use of the overall capital that you have, and over what time can we expect it to be used?

Alan Stewart:

This is Alan. I think, when we filed the shelf, it was based on, we think, excellent advice as good corporate governance to do so. I would say to the extent that we do need cash or need it in—outside of our operating cash that we have on board, it would be related to some sort of an acquisition, a tuck-in acquisition as well. That will be the primary use of cash outside of operations.

Saliq Khan:

Got it. The last from my end is one of the things I've noted to other folks and I believe I have noted to you as well, is that I think being in the drone business could be very meaningful. One of the things that I noticed recently was Taser, or Axon as they are known now, they announced a partnership with DJI to be able to equip the police officers with a lot of the drones and a lot of the analytical capabilities. How do you think about that? Is that a threat? Is that a potential opportunity? How do you view that partnership, and could we expect something similar from you guys as well?

Alan Stewart:

No comment on that specific partnership. But I will say that we're finding the UAV integration with ShotSpotter space a very interesting one. I think you might be aware that the city of Louisville had applied for a Bloomberg philanthropy grant to basically test the idea of combining our ShotSpotter alert with a UAV response, where you could basically put eyes on target in the day time or in the evening time. We're pretty excited and bullish on that and are looking forward to working with the Louisville PD on that implementation.

Saliq Khan:

Great. Thank you, guys.

Alan Stewart:

Thank you, Saliq.

Operator:

The next question is from Jaeson Schmidt with Lake Street Capital Markets. Please proceed.

Jaeson Schmidt:

Hey, guys. Thanks for taking my questions. Wondering if you could update us on how the rollout in Chicago is progressing?

Alan Stewart:

Sure. This is Alan. The rollout in Chicago is complete at this point. There's over 100 miles that have been deployed. And we're actually currently working on a multiyear contract with Chicago, which we think will be quite interesting when it gets executed. It will not only increase our deferred revenue significantly once it's executed by both parties, it's already been fully negotiated. We've signed it and we're just waiting on counter signatures. That contract is for three years with the two one-year base periods on top of that and has a price in excess of \$20 million.

Jaeson Schmidt:

Okay. How should we think about the NRE fees going forward? I know you mentioned there was about \$0.5 million in Q2. Is that going to remain somewhat consistent in future quarters?

Alan Stewart:

The NRE is periodic in nature. It's related to the Verizon technology integration. You may recall last year, we had a similar integration with GE. It is not going to be something we're going to see every quarter.

Jaeson Schmidt:

Okay. The last one from me and then I'll jump back into queue, I know grants such as Baltimore have been increasingly visible. Can you just talk about—if you're seeing increased inbound interest from these sources of funding?

Ralph Clark:

Oh, from philanthropy funding? Is that your question?

Jaeson Schmidt:

Yes.

Ralph Clark:

Oh, I'm sorry. This is Ralph. I think we're increasingly seeing more collaboration amongst agencies and kind of the private sector to fund ShotSpotter implementations. We've had some recent successes in getting local trauma hospitals, as an example, to defray some of the cost of ShotSpotter because they see the value in helping the police departments be more responsive to incidents of gun violence. It also happens to be where a lot of their employees live in some of these at-risk neighborhoods. As a corporate citizen, good corporate citizen role, we're seeing people having much more interest, or institutions, much more interest in helping fund ShotSpotter deployments.

Jaeson Schmidt:

Okay. Thanks a lot, guys.

Ralph Clark:

Thank you.

Alan Stewart:

Thank you.

Operator:

The next question is from Jeremy Hamblin with Dougherty & Company. Please proceed.

Jeremy Hamblin:

Hey, guys. I will add my congratulations on the strong results. I wanted to start out by asking you to confirm on the sales and marketing, R&D, G&A, I think what you indicated was we'll see some sequential dollar growth in each of those categories the remainder of the year. Did I catch that correctly?

Ralph Clark:

That's correct, yes.

Jeremy Hamblin:

Okay. Then, in terms of kind of phenomenal performance here and profitability improvement, on the sales and marketing side, you saw a pretty solid jump there on your total dollars spent. How much of that was increased staffing levels versus, let's say, incentive compensation going along with getting 61 net new live miles?

Alan Stewart:

This is Alan. I would say that there is a mix. We have added to our sales and marketing staff, both in the direct sales side over the last year. We've also added, which goes into that number on the customer success side over the last year, as well as adding to the marketing team as well. All three of those who roll up into the sales and marketing and there are associated compensation or commissions that do go along with some of those as well.

Jeremy Hamblin:

Okay, fantastic. In terms of the marketing efficiency that you are seeing, you've seen a significant improvement. I think you measure that on a kind of per dollar of revenue generated. I know it has kind of ranged in the \$0.28 to \$0.34 of sales and marketing spend. How has that been tracking the first half of the year or maybe Q3 specifically—Q2, excuse me?

Alan Stewart:

This is Alan. We don't track it by quarter. I would expect by the end of the year to be similar.

Jeremy Hamblin:

Okay. Then, what about in terms of installation costs? You obviously had a lot going on here in the last few months. You noted on Q1 that you had seen a little bit of a decline in your install costs, in particular, telecom costs. What are you seeing now? I mean, we've seen—started to see some inflationary pressures in other pockets of business. What have you seen on that side of your operations?

Alan Stewart:

Yes, great question. This is Alan again. We are seeing that our costs are being—we're actually being more efficient in not only on the deployments themselves, the partners we work with, but some of the actual telcom costs are going down as well. That is also benefiting us from a gross margin perspective. We do expect that to continue. At some point though, it will probably hit a limit where the efficiencies are going to be all what we're going to get.

Jeremy Hamblin:

Understood. In terms of, just coming back to the gross margin, the assumption would be your gross margin should track at least at Q2 levels the remainder of the year, but possibly a little bit better. Should our assumption be that sales and marketing, you're going to see some deleverage in Q3, and then maybe not as much deleverage in Q4? Because last year, you had a kind of a one-off much higher number in Q4?

Alan Stewart:

I would say that we're going to see smaller overall increases on a percentage basis in all of our operating expenses, pretty much from here on out. We will have marginal dollar increases in each of those but less than we're seeing our revenue increasing.

Jeremy Hamblin:

Okay. Then, last question. In terms of this bogey of kind of a \$10 million quarterly revenue run rate that I think you've indicated that you would expect profitability at that level, has that number changed at all in terms of that bogey of where you would expect profitability? Has it come down? Or has it gone up at all in terms of operationally what you need to get to profitability?

Alan Stewart:

That's an excellent question. This is Alan. We were—we almost hit profitable this quarter, got profitability. I would say, in our estimation, that number has come down slightly.

Jeremy Hamblin:

Great. Thanks, guys, for—and good luck for the rest of the year.

Alan Stewart:

Thank you.

Ralph Clark:

Thank you.

Operator:

The next question is from Joe Osha with JMP Securities. Please proceed.

Joseph Osha:

Hello there, gentlemen.

Ralph Clark:

Good afternoon.

Joseph Osha:

Hey, just fine. I wanted to go back if I could to this question of the composition of business. We talked about Chicago a bit. Was Chicago pretty much the source of all the existing customer growth that we saw this quarter or was there someone else? I'm kind of factoring into a broader question here, which is if you can give us some sense as to the new versus existing customer breakdown on the quarter?

Ralph Clark:

This is Ralph. I think in the prepared remarks, we talked about adding two new cities as a part of that 61 miles going live, Baltimore and Calumet City. The rest were expansions from a combination of Chicago, New York City and Miami and a little bit of Springfield.

Joseph Osha:

Would it be fair to say that those two new cities are probably pretty small, kind of three- to five-mile type of thing?

Ralph Clark:

Yes, that would be very fair to say that.

Joseph Osha:

Okay. I believe, as we've spoken in the past, that you guys have said that you would expect over time this business to swing a little bit more back towards new customers as a percentage of the total, as you move through the remainder of this year and into next. Is that still true?

Ralph Clark:

Yes, I think that's a fair characterization.

Joseph Osha:

Okay, all right. Thank you very much. Sorry if I'm hard to hear. I'm trying my new app Apple AirPods here so.

Ralph Clark:

It works just fine. We can hear you fine.

Joseph Osha:

Okay, all right. That's good, that's good to know.

Operator:

The next question comes from Rob Stone from Cowen and Company. Please proceed.

Robert Stone:

Hi, guys. I just wanted to start with a clarification question for Alan. I think you mentioned that the combination of catch-up and NRE in the quarter was about \$0.5 million in total. But am I correct in assuming that the bigger portion of that, that was catch-up as opposed to NRE? NRE is not anything like—it's about \$0.5 million, correct?

Alan Stewart:

No, you're correct. Less than half of that was NRE.

Robert Stone:

Okay. On the subject of the Smart Cities, do you have a sense of sort of the decline or what other milestones we should be looking for? When do Smart Cities' deployments start to become visible for you?

Ralph Clark:

Yes. This is Ralph. We had our first Smart City deployment with GE Current in Atlanta, and we see a lot of activity with GE Current also with Verizon. We're obviously working with Verizon, integrating our sensor technology into their Smart City, Intelligent City infrastructure. This is an area where there's a lot of, I guess, marketing chatter. We don't have, in our current thinking in our plan, any real revenues associated with that for this year. But my hope and expectation is that we would see some amount of revenue contribution from Smart Cities in 2019 and beyond.

Alan Stewart:

This is Alan. I would just add that we are seeing an increasing amount of activity from all of our Smart City partners. Although we remain cautiously optimistic, I think it's more cautious in timing in terms of when that's actually going to produce teaming relationships, actual contracts and revenue.

Robert Stone:

That was going to be my follow-up, which I guess, this is to a large extent, with the exception of Atlanta I guess, it's all breaking new ground. I would imagine you could have a situation where the infrastructure gets deployed but the decision on turning on the ShotSpotter services is maybe on a separate parallel path with different timing and different hurdles to cross. Is that fair?

Ralph Clark:

Sure. I mean, I think that's one path. But frankly, I think another path, and Atlanta is a great example of this, is we are the tail kind of wagging the dog, I think, from a Smart City infrastructure point of view. That was the application that the city was most interested in. I think it can happen either way.

Robert Stone:

Okay. Just to remind us, the deployment cost in a Smart City context is what, in proportion to when you have to put up a sensor network without any infrastructure being deployed for a Smart City? I'm not looking for an exact number. I just need a proportion.

Alan Stewart:

Sure. Yes, this is Alan. I think what we're finding, as we even scope out additional potential Smart City projects, is there is going to be a varying number of the Smart City-enabled nodes versus the ShotSpotter

sensors. To the extent that there's more sensors that are required to have adequate acoustic coverage, the cost will be more similar to our current Flex deployments. To the extent where there's much less or maybe only one or two, then the cost would go significantly down because we wouldn't be deploying a lot of the infrastructure. It would be the Smart City vendor.

Robert Stone:

Great. We'll look forward to more on that next year. On the indoor sensors, I think the press release mentioned that you're evaluating what to do with the remaining inventory. If you were going to seek a partner for this stuff, is that something you could potentially pass along to someone that way?

Alan Stewart:

Sure. This is Alan. We are looking at partners in that, that are focused on the indoor sensor. The Shooter Detection Systems is one company that we are looking at. Really, it will be when we are asked to provide, not just the outdoor coverage but let's say they also want indoor coverage, that's when we would bring someone else along. We haven't seen a lot of that. But if that were to be presented to us, we would look to partner with someone like them.

Robert Stone:

Okay, and one last kind of housekeeping question. You mentioned that OpEx was going to be up in dollars in each of the subcategories. But G&A was actually down sequentially from Q1 and a bit. Any color there?

Alan Stewart:

Sure. Yes, it's—in Q1, we had some G&A costs that were related to the ongoing litigation. We have reached what we would call our retention amount at this point, so those costs are no longer flowing through our income statement.

Robert Stone:

Okay. That's all I have. Thank you very much.

Ralph Clark:

Thank you.

Alan Stewart:

Great question. Thank you.

Operator:

At this time, this concludes our question-and-answer session. If your question was not taken, you may contact ShotSpotter's Investor Relations team at SSTI@liolios.com. I would now like to turn the call back over to Mr. Clark for his closing remarks.

Ralph Clark:

Great. Thank you very much, everyone, for joining us on this quarterly earnings' call. We're enormously grateful for all the support we're getting from our investors and analysts covering the Company and trying to understand the business that we're in. We're also grateful to do the work that we do with these policing

agencies throughout United States and helping them address gun violence in our most vulnerable communities. Looking forward to seeing you all on the next earnings call. Thanks.

Operator:

Thank you for joining us today for ShotSpotter's Second Quarter 2018 Earnings Call. You may now disconnect.