

Zscaler Reports Third Quarter Fiscal 2020 Financial Results

- Revenue grows 40% year-over-year to \$110.5 million
- Calculated billings grow 55% year-over-year to \$131.3 million
- Deferred revenue grows 42% year-over-year to \$300.8 million
- GAAP net loss of \$19.3 million compared to GAAP net loss of \$12.2 million on a year-over-year basis
- Non-GAAP net income of \$9.0 million compared to non-GAAP net income of \$7.4 million on a year-over-year basis

SAN JOSE, California. - May 28, 2020 - Zscaler, Inc. (Nasdaq: ZS), the leader in cloud security, today announced financial results for its third quarter of fiscal year 2020, ended April 30, 2020.

"Our strong results are a reflection of our sales execution and the entire Zscaler team stepping up to help our customers succeed in these difficult times. The mitigation activities taken by every enterprise in response to the COVID-19 pandemic created an immediate need for strong security and access to the internet and business applications, all while working from anywhere," said Jay Chaudhry, Chairman and CEO of Zscaler. "The digital transformation that is driving our business is further accelerating, and we believe the Zscaler cloud security platform is best positioned to help our customers thrive no matter where their teams are working."

Third Quarter Fiscal 2020 Financial Highlights

- **Revenue:** \$110.5 million, an increase of 40% year-over-year.
- **Income (loss) from operations:** GAAP loss from operations was \$20.5 million, or 19% of total revenue, compared to \$13.5 million, or 17% of total revenue, in the third quarter of fiscal 2019. Non-GAAP income from operations was \$8.3 million, or 8% of total revenue, compared to \$6.1 million, or 8% of total revenue, in the third quarter of fiscal 2019.
- **Net income (loss):** GAAP net loss was \$19.3 million, compared to \$12.2 million in the third quarter of fiscal 2019. Non-GAAP net income was \$9.0 million, compared to \$7.4 million in the third quarter of fiscal 2019.
- **Net income (loss) per share:** GAAP net loss per share was \$0.15, compared to \$0.10 in the third quarter of fiscal 2019. Non-GAAP net income per share was \$0.07, compared to \$0.05 in the third quarter of fiscal 2019.
- **Cash flow:** Cash provided by operations was \$20.8 million, or 19% of revenue, compared to \$13.5 million, or 17% of revenue, in the third quarter of fiscal 2019. Free cash flow was \$9.1 million, or 8% of revenue, compared to \$4.6 million, or 6% of revenue, in the third quarter of fiscal 2019.
- **Deferred revenue:** \$300.8 million as of April 30, 2020, an increase of 42% year-over-year.
- **Cash, cash equivalents and short-term investments:** \$391.3 million as of April 30, 2020, an increase of \$26.7 million from July 31, 2019.

Recent Business Highlights

- Supported Zscaler customers, allowing their employees to work from home to maintain business continuity throughout the COVID-19 pandemic. Since February, Zscaler Private Access (ZPA) traffic grew over 10x and the Zscaler Cloud Security Platform reached a new milestone of securing 100 billion transactions per day.
- In April 2020, Zscaler acquired Cloudneeti Corporation, a cloud security posture management (CSPM) company which prevents and remediates misconfigurations of applications in SaaS, IaaS and PaaS.
- In May 2020, Zscaler acquired Edgewise Networks, a pioneer in securing application-to-application communications in public clouds and data centers. Edgewise customers measurably reduce the attack surface to lower the risk of application compromise and data breaches by simplifying the security of east-west communications through identity-based segmentation.

- Launched the Zscaler Summit Partner Program to help customers and prospects achieve secure digital transformation by fostering tighter collaboration with partners. The program will create long-term partner growth by expanding opportunities and providing the training that partners need to become trusted advisors to customers.
- Revealed results from the company's second annual Internet of Things (IoT) ThreatLabZ research report, IoT Devices in the Enterprise 2020: Shadow IoT Threat Emerges. The research findings included a startling rise in employees bringing unauthorized devices into the enterprise.
- Named one of the 2020 Bay Area's Best Places to Work by the San Francisco Business Times and Silicon Valley Business Journal.

Financial Outlook

For the fourth quarter of fiscal 2020, we expect:

- Total revenue of \$117 million to \$119 million
- Non-GAAP income from operations of \$2 million to \$4 million
- Non-GAAP earnings per share of approximately \$0.02 to \$0.03, assuming approximately 140 million common shares outstanding

For the full year fiscal 2020, we expect:

- Total revenue of \$422 million to \$424 million
- Calculated billings of \$529 million to \$531 million
- Non-GAAP income from operations of \$24 million to \$26 million
- Non-GAAP earnings per share of \$0.20 to \$0.21, assuming approximately 138 million common shares outstanding

These statements are forward-looking and actual results may differ materially. Refer to the Forward-Looking Statements safe harbor below for information on the factors that could cause our actual results to differ materially from these forward-looking statements.

Guidance for non-GAAP financial measures excludes stock-based compensation expense, amortization expense of acquired intangible assets, asset impairment related to facility exit, certain litigation-related expenses and income tax effects generated by intangible assets acquired in business acquisitions. We have not reconciled our expectations to non-GAAP income from operations and non-GAAP net income per share to their most directly comparable GAAP measures because certain items are out of our control or cannot be reasonably predicted. Accordingly, a reconciliation for non-GAAP income from operations and non-GAAP net income per share is not available without unreasonable effort.

Conference Call and Webcast Information

Zscaler will host a conference call for analysts and investors to discuss its third quarter fiscal 2020 earnings results and outlook for its fourth quarter of fiscal 2020 and full year fiscal 2020 today at 1:30 p.m. Pacific time (4:30 p.m. Eastern time).

Date: Thursday, May 28, 2020
Time: 1:30 p.m. PT
Webcast: <https://ir.zscaler.com/>
Dial-in number: 918-922-3018

Upcoming Conferences

Fourth Quarter of Fiscal 2020 Virtual Investor Conference Participation Schedule:

- Cowen 2020 Technology, Media & Telecom Conference
Friday, May 29, 2020
- Bank of America 2020 Global Technology Conference

Wednesday, June 3, 2020

- Baird 2020 Virtual Global Consumer, Technology & Services Conference
Thursday, June 4, 2020
- Morgan Stanley – “Zero Trust Architectures” Thematic Virtual Conference
Thursday, June 25, 2020

Zscaler's conference presentations are expected to be available via webcast on the Investor Relations section of the company's website. To hear these presentations and to access the most updated information, please visit the Investor Relations section of Zscaler's website at <https://ir.zscaler.com>.

Forward-Looking Statements

This press release contains forward-looking statements that involve risks and uncertainties, including statements regarding our future financial and operating performance, including our financial outlook for the fourth quarter of fiscal 2020 and full year fiscal 2020. There are a significant number of factors that could cause actual results to differ materially from statements made in this press release, including but not limited to: the duration and global impact of COVID-19 on our business, operations and financial results and the economy in general; our ability as an organization to acquire and integrate other companies, products or technologies in a successful manner; our limited operating history; our ability to identify and effectively implement the necessary changes to address execution challenges; risks associated with managing our rapid growth, including fluctuations from period to period; our limited experience with new product and subscription and support introductions and the risks associated with new products and subscription and support offerings, including the discovery of software bugs; our ability to attract and retain new customers; the failure to timely develop and achieve market acceptance of new products and subscriptions as well as existing products and subscription and support; rapidly evolving technological developments in the market for network security products and subscription and support offerings and our ability to remain competitive; length of sales cycles; and general market, political, economic and business conditions.

Additional risks and uncertainties that could affect our financial results are included under the captions “Risk Factors” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” set forth from time to time in our filings and reports with the Security Exchange Commission (SEC), including our Annual Report on Form 10-K for the fiscal year ended July 31, 2019 filed on September 18, 2019, as well as future filings and reports by us, copies of which are available on our website at ir.zscaler.com and on the SEC’s website at www.sec.gov. Additional information will also be set forth on our Quarterly Report on Form 10-Q that will be filed for the fiscal quarter ended April 30, 2020, which should be read in conjunction with this press release and the financial results included herein. You should not rely on these forward-looking statements, as actual outcomes and results may differ materially from those contemplated by these forward-looking statements as a result of such risks and uncertainties. Additional information will also be set forth in other filings that we make with the SEC from time to time. All forward-looking statements in this press release are based on information available to us as of the date hereof, and we do not assume any obligation to update the forward-looking statements provided to reflect events that occur or circumstances that exist after the date on which they were made.

Use of Non-GAAP Financial Information

We believe that the presentation of non-GAAP financial information provides important supplemental information to management and investors regarding financial and business trends relating to our financial condition and results of operations. For further information regarding why we believe that these non-GAAP measures provide useful information to investors, the specific manner in which management uses these measures, and some of the limitations associated with the use of these measures, please refer to the “Explanation of Non-GAAP Financial Measures” section of this press release.

About Zscaler

Zscaler enables the world's leading organizations to securely transform their networks and applications for a mobile and cloud-first world. Its flagship services, Zscaler Internet Access™ and Zscaler Private Access™, create fast, secure connections between users and applications, regardless of device, location, or network. Zscaler services are 100 percent cloud-delivered and offer the simplicity, enhanced security and improved user experience that traditional appliances are unable to match. Used in more than 185 countries, Zscaler operates a multi-tenant distributed cloud security platform, protecting thousands of customers from cyberattacks and data loss. Learn more at zscaler.com or follow us on Twitter @zscaler.

Zscaler™, Zscaler Internet Access™, and Zscaler Private Access™, ZIA™ and ZPA™ are either (i) registered trademarks or service marks or (ii) trademarks or service marks of Zscaler, Inc. in the United States and/or other countries. Any other trademarks are the properties of their respective owners.

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ZSCALER, INC.
Condensed Consolidated Statements of Operations
(in thousands, except per share amounts)
(unaudited)

| | Three Months Ended | | Nine months ended | |
|---|--------------------|-------------|-------------------|-------------|
| | April 30, | | April 30, | |
| | 2020 | 2019 | 2020 | 2019 |
| Revenue | \$ 110,524 | \$ 79,128 | \$ 305,382 | \$ 216,728 |
| Cost of revenue ⁽¹⁾⁽²⁾ | 24,579 | 14,960 | 64,375 | 42,330 |
| Gross profit | 85,945 | 64,168 | 241,007 | 174,398 |
| Operating expenses: | | | | |
| Sales and marketing ⁽¹⁾⁽²⁾ | 67,727 | 45,295 | 188,759 | 120,596 |
| Research and development ⁽¹⁾⁽²⁾ | 24,117 | 16,499 | 65,094 | 44,756 |
| General and administrative ⁽¹⁾⁽³⁾⁽⁴⁾ | 14,615 | 15,911 | 56,223 | 36,428 |
| Total operating expenses | 106,459 | 77,705 | 310,076 | 201,780 |
| Loss from operations | (20,514) | (13,537) | (69,069) | (27,382) |
| Interest income | 1,528 | 2,081 | 5,405 | 5,595 |
| Other income (expense), net | 70 | (144) | 28 | (82) |
| Loss before income taxes | (18,916) | (11,600) | (63,636) | (21,869) |
| Provision for income taxes | 421 | 636 | 1,931 | 1,510 |
| Net loss | \$ (19,337) | \$ (12,236) | \$ (65,567) | \$ (23,379) |
| Net loss per share, basic and diluted | \$ (0.15) | \$ (0.10) | \$ (0.51) | \$ (0.19) |
| Weighted-average shares used in computing net loss per share, basic and diluted | 129,682 | 124,672 | 128,538 | 122,644 |

⁽¹⁾ Includes stock-based compensation expense as follows:

| | | | | |
|----------------------------|-----------|-----------|-----------|-----------|
| Cost of revenue | \$ 1,614 | \$ 686 | \$ 4,575 | \$ 1,808 |
| Sales and marketing | 15,119 | 6,459 | 37,101 | 14,777 |
| Research and development | 6,738 | 4,194 | 17,689 | 11,387 |
| General and administrative | 4,299 | 1,936 | 10,647 | 6,116 |
| Total | \$ 27,770 | \$ 13,275 | \$ 70,012 | \$ 34,088 |

⁽²⁾ Includes amortization expense of acquired intangible assets as follows:

| | | | | |
|--------------------------|--------|--------|----------|--------|
| Cost of revenue | \$ 348 | \$ 163 | \$ 758 | \$ 307 |
| Sales and marketing | 8 | 3 | 24 | 3 |
| Research and development | 285 | — | 1,280 | 95 |
| Total | \$ 641 | \$ 166 | \$ 2,062 | \$ 405 |

⁽³⁾ Includes asset impairment related to facility exit as follows: \$ 430 \$ — \$ 746 \$ —

⁽⁴⁾ Includes litigation-related expenses as follows: \$ 12 \$ 6,164 \$ 18,353 \$ 10,106

ZSCALER, INC.
Condensed Consolidated Balance Sheets
(in thousands)
(unaudited)

| | April 30, 2020 (*) | July 31, 2019 |
|---|-------------------------------------|--------------------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 124,592 | \$ 78,484 |
| Short-term investments | 266,722 | 286,162 |
| Accounts receivable, net | 105,583 | 93,341 |
| Deferred contract acquisition costs | 26,316 | 21,219 |
| Prepaid expenses and other current assets | 28,903 | 16,880 |
| Total current assets | 552,116 | 496,086 |
| Property and equipment, net | 63,297 | 41,046 |
| Operating lease right-of-use assets | 35,128 | — |
| Deferred contract acquisition costs, noncurrent | 58,024 | 48,566 |
| Acquired intangible assets, net | 10,146 | 8,708 |
| Goodwill | 13,350 | 7,479 |
| Other noncurrent assets | 3,903 | 2,277 |
| Total assets | <u>\$ 735,964</u> | <u>\$ 604,162</u> |
| Liabilities and Stockholders' Equity | | |
| Current liabilities: | | |
| Accounts payable | \$ 9,392 | \$ 6,208 |
| Accrued expenses and other current liabilities | 14,366 | 12,810 |
| Accrued compensation | 34,215 | 21,544 |
| Deferred revenue | 274,726 | 221,387 |
| Operating lease liabilities | 12,939 | — |
| Total current liabilities | 345,638 | 261,949 |
| Deferred revenue, noncurrent | 26,065 | 29,815 |
| Operating lease liabilities, noncurrent | 27,909 | — |
| Other noncurrent liabilities | 1,558 | 3,840 |
| Total liabilities | 401,170 | 295,604 |
| Stockholders' Equity | | |
| Common stock | 130 | 127 |
| Additional paid-in capital | 623,859 | 532,618 |
| Accumulated other comprehensive income | 827 | 268 |
| Accumulated deficit | (290,022) | (224,455) |
| Total stockholders' equity | 334,794 | 308,558 |
| Total liabilities and stockholders' equity | <u>\$ 735,964</u> | <u>\$ 604,162</u> |

(*) On August 1, 2019, we adopted Topic 842 using the transition option that allows to be applied prospectively at the beginning of the fiscal year of adoption. As such, the condensed consolidated balance sheets for prior periods are not comparable to our fiscal 2020 periods. The adoption of this standard resulted in the recognition of the operating lease right-of-use assets and operating lease liabilities related to our real estate and co-location arrangements.

ZSCALER, INC.
Condensed Consolidated Statements of Cash Flows
(in thousands)
(unaudited)

Nine Months Ended
April 30,

2020 **2019**

Cash Flows From Operating Activities

| | | |
|---|-------------------|------------------|
| Net loss | \$ (65,567) | \$ (23,379) |
| Adjustments to reconcile net loss to cash provided by operating activities | | |
| Depreciation and amortization expense | 12,278 | 7,331 |
| Impairment of assets | 746 | — |
| Amortization expense of acquired intangible assets | 2,062 | 405 |
| Amortization of deferred contract acquisition costs | 17,673 | 13,505 |
| Noncash operating lease costs | 9,649 | — |
| Stock-based compensation expense | 70,012 | 34,088 |
| Deferred income taxes | (555) | — |
| Accretion of purchased discounts, net of amortization of investment premiums | (463) | (1,702) |
| Other | 305 | 244 |
| Changes in operating assets and liabilities, net of effects of business acquisitions: | | |
| Accounts receivable | (12,218) | (9,540) |
| Deferred contract acquisition costs | (32,228) | (21,700) |
| Prepaid expenses, other current and noncurrent assets | (13,365) | (3,361) |
| Accounts payable | 1,923 | (611) |
| Accrued expenses, other current and noncurrent liabilities | 660 | (1,047) |
| Accrued compensation | 12,671 | (1,548) |
| Deferred revenue | 49,581 | 47,519 |
| Operating lease liabilities | (5,482) | — |
| Net cash provided by operating activities | 47,682 | 40,204 |
| Cash Flows From Investing Activities | | |
| Purchases of property, equipment and other assets | (24,793) | (16,698) |
| Capitalized internal-use software | (6,296) | (1,713) |
| Acquired intangible assets | — | (1,480) |
| Payments for business acquisitions, net of cash acquired | (8,918) | (823) |
| Purchases of short-term investments | (202,764) | (272,324) |
| Proceeds from maturities of short-term investments | 209,225 | 139,361 |
| Proceeds from sale of short-term investments | 14,084 | — |
| Net cash used in investing activities | (19,462) | (153,677) |
| Cash Flows From Financing Activities | | |
| Payments of offering costs related to initial public offering | — | (1,797) |
| Proceeds from issuance of common stock upon exercise of stock options | 12,554 | 23,523 |
| Proceeds from issuance of common stock under the employee stock purchase plan | 5,334 | 8,691 |
| Repurchases of unvested common stock | — | (22) |
| Repayments of notes receivable from stockholders | — | 1,905 |
| Net cash provided by financing activities | 17,888 | 32,300 |
| Net increase (decrease) in cash, cash equivalents and restricted cash | 46,108 | (81,173) |
| Cash, cash equivalents and restricted cash at beginning of period | 78,484 | 136,147 |
| Cash, cash equivalents and restricted cash at end of period | \$ 124,592 | \$ 54,974 |
| Reconciliation of cash, cash equivalents and restricted cash to the condensed consolidated balance sheets: | | |
| Cash and cash equivalents | \$ 124,592 | \$ 54,974 |
| Restricted cash, current and non-current | — | — |
| Total cash, cash equivalents and restricted cash | \$ 124,592 | \$ 54,974 |

ZSCALER, INC.
Reconciliation of GAAP to Non-GAAP Financial Measures

(in thousands)

(unaudited)

| | Three Months Ended | | Nine Months Ended | |
|--|--------------------|-------------|-------------------|-------------|
| | April 30, | | April 30, | |
| | 2020 | 2019 | 2020 | 2019 |
| Revenue | \$ 110,524 | \$ 79,128 | \$ 305,382 | \$ 216,728 |
| Non-GAAP Gross Profit and Non-GAAP Gross Margin | | | | |
| GAAP gross profit | \$ 85,945 | \$ 64,168 | \$ 241,007 | \$ 174,398 |
| Add: | | | | |
| Stock-based compensation expense | 1,614 | 686 | 4,575 | 1,808 |
| Amortization expense of acquired intangible assets | 348 | 163 | 758 | 307 |
| Non-GAAP gross profit | \$ 87,907 | \$ 65,017 | \$ 246,340 | \$ 176,513 |
| GAAP gross margin | 78 % | 81 % | 79 % | 80 % |
| Non-GAAP gross margin | 80 % | 82 % | 81 % | 81 % |
| Non-GAAP Income from Operations and Non-GAAP Operating Margin | | | | |
| GAAP loss from operations | \$ (20,514) | \$ (13,537) | \$ (69,069) | \$ (27,382) |
| Add: | | | | |
| Stock-based compensation expense | 27,770 | 13,275 | 70,012 | 34,088 |
| Litigation-related expenses | 12 | 6,164 | 18,353 | 10,106 |
| Amortization expense of acquired intangible assets | 641 | 166 | 2,062 | 405 |
| Asset impairment related to facility exit ⁽¹⁾ | 430 | — | 746 | — |
| Non-GAAP income from operations | \$ 8,339 | \$ 6,068 | \$ 22,104 | \$ 17,217 |
| GAAP operating margin | (19)% | (17)% | (23)% | (13)% |
| Non-GAAP operating margin | 8 % | 8 % | 7 % | 8 % |

⁽¹⁾ Consists of asset impairment charges related to the relocation of our corporate headquarters.

ZSCALER, INC.
Reconciliation of GAAP to Non-GAAP Financial Measures
(in thousands, except per share amounts)
(unaudited)

| | Three Months Ended | | Nine Months Ended | |
|--|--------------------|-----------------|-------------------|------------------|
| | April 30, | | April 30, | |
| | 2020 | 2019 | 2020 | 2019 |
| Non-GAAP Net Income per Share, Diluted | | | | |
| GAAP net loss | \$ (19,337) | \$ (12,236) | \$ (65,567) | \$ (23,379) |
| Stock-based compensation expense | 27,770 | 13,275 | 70,012 | 34,088 |
| Litigation-related expenses | 12 | 6,164 | 18,353 | 10,106 |
| Amortization expense of acquired intangible assets | 641 | 166 | 2,062 | 405 |
| Asset impairment related to facility exit ⁽¹⁾ | 430 | — | 746 | — |
| Provision for income taxes ⁽²⁾ | (490) | — | (490) | — |
| Non-GAAP net income | <u>\$ 9,026</u> | <u>\$ 7,369</u> | <u>\$ 25,116</u> | <u>\$ 21,220</u> |
| | | | | |
| GAAP net loss per share, diluted | \$ (0.15) | \$ (0.10) | \$ (0.51) | \$ (0.19) |
| Stock-based compensation expense | 0.20 | 0.10 | 0.51 | 0.25 |
| Litigation-related expenses | — | 0.05 | 0.13 | 0.07 |
| Amortization expense of acquired intangible assets | — | — | 0.02 | — |
| Asset impairment related to facility exit ⁽¹⁾ | — | — | 0.01 | — |
| Provision for income taxes ⁽²⁾ | — | — | — | — |
| Adjustment to total fully diluted earnings per share ⁽³⁾ | 0.02 | — | 0.02 | 0.03 |
| Non-GAAP net income per share, diluted | <u>\$ 0.07</u> | <u>\$ 0.05</u> | <u>\$ 0.18</u> | <u>\$ 0.16</u> |
| | | | | |
| Weighted-average shares used in computing non-GAAP net income per share, diluted | <u>137,873</u> | <u>136,538</u> | <u>137,218</u> | <u>135,159</u> |

⁽¹⁾ Consists of asset impairment charges related to the relocation of our corporate headquarters.

⁽²⁾ We use our GAAP provision for income taxes for purposes of determining our non-GAAP income tax expense. The difference between our GAAP and non-GAAP income tax expense represents the effects of stock-based compensation expense recognized in foreign jurisdictions and any income tax benefits associated with business combinations. The income tax benefit related to stock-based compensation expense included in the GAAP provision for income taxes was not material for all periods presented. In the fiscal quarter ended April 30, 2020, we recorded a tax benefit of \$0.5 million, associated with intangible assets recognized as a result of our acquisition of Cloudneeti Corporation.

⁽³⁾ The sum of the fully diluted earnings per share impact of individual reconciling items may not total to fully diluted Non-GAAP net income per share due to the basic share counts used to calculate the GAAP net loss per share differ from the fully diluted share counts used to calculate the non-GAAP net income per share and due to rounding of the individual reconciling items. The GAAP net loss per share calculation uses a lower share count as it excludes potentially dilutive shares, which are included in calculating the non-GAAP income per share.

ZSCALER, INC.
Reconciliation of GAAP to Non-GAAP Financial Measures
(in thousands)
(unaudited)

| | Three Months Ended | | Nine Months Ended | |
|---|--------------------|------------------|-------------------|-------------------|
| | April 30, | | April 30, | |
| | 2020 | 2019 | 2020 | 2019 |
| Calculated Billings | | | | |
| Revenue | \$ 110,524 | \$ 79,128 | \$ 305,382 | \$ 216,728 |
| Add: Total deferred revenue, end of period | 300,791 | 211,542 | 300,791 | 211,542 |
| Less: Total deferred revenue, beginning of period | (280,022) | (206,020) | (251,202) | (164,023) |
| Calculated billings | <u>\$ 131,293</u> | <u>\$ 84,650</u> | <u>\$ 354,971</u> | <u>\$ 264,247</u> |
| Free Cash Flow | | | | |
| Net cash provided by operating activities | \$ 20,822 | \$ 13,483 | \$ 47,682 | \$ 40,204 |
| Less: Purchases of property, equipment and other assets | (9,694) | (8,091) | (24,793) | (16,698) |
| Less: Capitalized internal-use software | (2,023) | (810) | (6,296) | (1,713) |
| Free cash flow | <u>\$ 9,105</u> | <u>\$ 4,582</u> | <u>\$ 16,593</u> | <u>\$ 21,793</u> |
| As a percentage of revenue: | | | | |
| Net cash provided by operating activities | 19 % | 17 % | 15 % | 19 % |
| Less: Purchases of property, equipment and other assets | (9)% | (10)% | (8)% | (8)% |
| Less: Capitalized internal-use software | (2)% | (1)% | (2)% | (1)% |
| Free cash flow margin | <u>8 %</u> | <u>6 %</u> | <u>5 %</u> | <u>10 %</u> |

ZSCALER, INC.
Explanation of Non-GAAP Financial Measures

In addition to our results determined in accordance with generally accepted accounting principles in the United States of America (GAAP), we believe the following non-GAAP measures are useful in evaluating our operating performance. We use the following non-GAAP financial information to evaluate our ongoing operations and for internal planning and forecasting purposes. We believe that non-GAAP financial information, when taken collectively, may be helpful to investors because it provides consistency and comparability with past financial performance. However, non-GAAP financial information is presented for supplemental informational purposes only, has limitations as an analytical tool and should not be considered in isolation or as a substitute for financial information presented in accordance with GAAP. In particular, free cash flow is not a substitute for cash used in operating activities. Additionally, the utility of free cash flow as a measure of our liquidity is further limited as it does not represent the total increase or decrease in our cash balance for a given period. In addition, other companies, including companies in our industry, may calculate similarly-titled non-GAAP measures differently or may use other measures to evaluate their performance, all of which could reduce the usefulness of our non-GAAP financial measures as tools for comparison. A reconciliation of the Company's historical non-GAAP financial measures to their most directly comparable financial measure stated in accordance with GAAP has been included in this press release. Investors are cautioned that there are a number of limitations associated with the use of non-GAAP financial measures and key metrics as analytical tools. Investors are encouraged to review these reconciliations, and not to rely on any single financial measure to evaluate our business.

Expenses Excluded from Non-GAAP Measures

Stock-based compensation expense is excluded primarily because they are non-cash expenses that management believes are not reflective of our ongoing operational performance. Amortization expense of acquired intangible assets is excluded because these are considered by management to be outside of the Company's core business operating performance. Asset impairments related to facility exit costs are excluded because such charges are not reflective of our ongoing operational performance. We also exclude certain litigation-related expenses consisting of professional fees and related costs incurred by us in defending against significant claims that we deem not to be in the ordinary course of our business and, if applicable, actual losses and accruals related to estimated losses in connection with these claims. There are many uncertainties and potential outcomes associated with any litigation, including the expense of litigation, timing of such expenses, court rulings, unforeseen developments, complications and delays, each of which may affect our results of operations from period to period, as well as the unknown magnitude of the potential loss relating to any lawsuit, all of which are inherently subject to change, difficult to predict and could adversely affect our results of operations. We estimate the tax effect of these items on our non-GAAP results and may adjust our GAAP provision for income taxes, if such effects have a material impact to our non-GAAP results.

Non-GAAP Financial Measures

Non-GAAP Gross Profit and Non-GAAP Gross Margin. We define non-GAAP gross profit as GAAP gross profit excluding stock-based compensation expense and amortization expense of acquired intangible assets. We define non-GAAP gross margin as non-GAAP gross profit as a percentage of revenue.

Non-GAAP Income from Operations and Non-GAAP Operating Margin. We define non-GAAP income from operations as GAAP loss from operations excluding stock-based compensation expense, amortization expense of acquired intangible assets, asset impairment related to facility exit and certain litigation-related expenses. We defined non-GAAP operating margin as non-GAAP income from operations as a percentage of revenue.

Non-GAAP Net Income per Share, Diluted. We define non-GAAP net income as GAAP net loss plus stock-based compensation expense, amortization expense of acquired intangible assets, asset impairment related to facility exit, certain litigation-related expenses, income tax effects generated by the effects of stock-based compensation expense recognized in foreign jurisdictions and any income tax benefits associated with business combinations. We define non-GAAP net income per share, diluted, as non-GAAP net income divided by the weighted-average diluted shares outstanding, which includes the dilutive effect of potentially diluted common stock equivalents outstanding during the period.

Free Cash Flow and Free Cash Flow Margin. We define free cash flow as net cash provided by operating activities less purchases of property, equipment and other and capitalized internal-use software. We define free cash flow margin as free cash flow divided by revenue. We believe that free cash flow and free cash flow margin are meaningful indicators of liquidity information to management and investors about the amount of cash generated from our operations that, after the investments in property, equipment and other and capitalized internal-use software, can be used for strategic initiatives.

Calculated Billings. We define calculated billings as total revenue plus the change in deferred revenue in a period. Calculated billings in any particular period aims to reflect amounts invoiced for subscriptions to access our cloud platform, together with related support services related to our new and existing customers. We typically invoice our customers annually in advance, and to a lesser extent quarterly in advance, monthly in advance or multi-year in advance.