# Blackline Safety Corp.
# Second Quarter 2023 Results
# Conference Call Transcript

**Date:** **June 14th, 2023**

**Time:** **9:00 AM MT / 11:00 AM ET**

**Speakers:**

**Scott Boston**
Vice President of Finance

**Cody Slater**
Chief Executive Officer & Chairman of the Board

**Shane Grennan**
Chief Financial Officer

**Operator:**

Welcome to the Blackline Safety Corp. Second Quarter 2023 Results Conference Call. (Operator Instructions)

I would now like to turn the conference over to Scott Boston, Vice President of Finance. Please go ahead.

**Scott Boston:**

Welcome, and thank you for joining us. Today we will be discussing our fiscal results for the second quarter, ended April 30, 2023, which were issued before market opening this morning.

With me today is Cody Slater, CEO and Chair of Blackline Safety Corp., as well as our CFO Shane Grennan. I will turn the call over to Cody in just a moment for an overview of our second quarter. Following that, Shane will discuss the financial highlights of the quarter in greater detail. Cody will then close with our outlook and some additional commentary before we take questions.

I'd like to remind everyone that this call is live and is being recorded today, Wednesday June 14, 2023. An archive of the webcast will be made available on the investors section of our website.

I'd like to note that some of the information discussed in this call is based on information as of today and contains forward-looking statements that involve risks and uncertainties. Actual results may differ materially from those set forth in such statements. For a discussion of these risks and uncertainties, please review the forward-looking statements disclosure in the earnings news release, as well as in the Company's SEDAR filings.

During this call, there will be a discussion of IFRS results, non-GAAP financial measures, non-GAAP ratios, and supplementary financial measures. A reconciliation between IFRS results and non-GAAP financial measures is available on the Company's earnings news release and MD&A, both of which can be found on our website, blacklinesafety.com, and on SEDAR. All dollar amounts are reported in Canadian dollars unless otherwise noted.

With that, I will now hand the call over to Mr. Slater.

**Cody Slater:**

Thank you Scott.

Good morning everyone, and welcome to Blackline Safety's second quarter 2023 conference call.

Q2 continued our strong momentum from the last several quarters, with another new record for total revenue of $24.1 million, which was up 45% year-over-year. This is our 25th consecutive quarter of year-over-year revenue growth. The rate of revenue growth also accelerated when compared to the first quarter of 2023, with service and product revenues up 46% and 43% respectively. We were able to achieve this while maintaining our reduced cost structure as we continue on our path to positive quarterly Adjusted EBITDA by the end of this fiscal year.

Q2 also set a record for gross margin, at $12.5 million, with an overall gross margin percentage of 52%, driven by our highest-ever service margin of 75%, which validates the opportunity for our business model to generate free cash flow in the near term.

At the end of the quarter, our annual recurring revenue had increased 38% year-over-year to $42.4 million, demonstrating the longer-term opportunity for Blackline as we scale our connected worker solution and our market share through customer adoption of our world-class products and services across a variety of industrial verticals.

We are seeing this growing success across all our regions, and we saw year-over-year revenue growth across the board, with our largest segment, United States, leading the way at 65%, including our recently announced win in Texas of a competitive bid for portable gas detection to protection 1,000 workers. Canada and Europe also remained strong, with 24% and 17% revenue growth respectively.

I want to specifically highlight the Rest of World, which increased 123%, achieving a new high-water mark with nearly $2 million in quarterly revenue. This team, now under the leadership of our new Vice President International Sales, Peter Attalla, is primed to continue driving the growth of Blackline in key international segments and increase the pipeline of deals from leading international energy, manufacturing, transportation, and chemical companies.

Within our service segment, we saw another quarter of extremely strong results from our rental team, generating $1.6 million in revenue, a 247% increase year-over-year. This rental offering not only provides incremental high-margin revenue from the industrial turn-around and construction markets, but it also enables companies who are not yet customers to experience the advantages of the Blackline solution at their facilities, and is a strong leading indicator for future sales.

Would also like to highlight our net dollar retention, which surpassed our earlier goal to reach 115% by the year end, coming in at 118% in Q2, up from 102% last Q2. We are now targeting 120% for this metric by our fiscal year end, as more customers renew their contracts with incremental service at a higher average revenue per unit.

All of this contributed to reducing our Adjusted EBITDA loss by 73%, from $12.3 million in Q2 of 2022 to $3.3 million in the current quarter, normalizing for the effects of foreign exchange gains. This demonstrates how far we are down the path to our goal of achieving quarterly positive Adjusted EBITDA by the end of fiscal 2023.

We maintained our solid financial position at the end of the quarter with total cash and short-term investments on hand of $21 million, including $8.3 million of funding received from the sale of the initial tranche of lease contracts under our new securitization agreement with CWB Maxium. With $15 million CAD and $35 million USD in total availability, this facility provides us with the opportunity to more aggressively market our all-in monthly solutions, which continue to be attractive to many customers, including those for our newest product line, the G6. As it relates to the G6, we've seen strong customer interest in the product and its roadmap. This has generated a robust pipeline, with the majority of customers looking for enhanced services on the roadmap that were not available at the launch of the product, but will be available in the fourth quarter of this fiscal year. While this will result in the delay of volume shipments anticipated in Q3, the G6 should be on track in Q4.

I would note that the short-term impact here is offset by the success we've had in the market penetration of our core products and resulting growth in our ARR. In the longer term, the opportunity to monetize these higher-value services for the G6 will create an even stronger product line for Blackline and its customers.

I will now turn the call over to our CFO, Shane Grennan, to discuss our fiscal second quarter results and financial position in more detail.

**Shane Grennan:**

Thank you Cody, and good morning all.

As Cody mentioned, we achieved our 25th consecutive quarter of year-over-year revenue growth of 45%, generating total revenue of $24.1 million. This includes $11.2 million in product revenue, which increased 43% year-over-year. Increase in the current year reflects the investments in the Company's expanded sales network and global sales team in the prior year, with continued strong demand generation and sales development activities.

Product gross margin percentage in the second quarter doubled to 26% from 13% in the prior year period. Product margin also increased sequentially from the first quarter, as we saw the benefits from our pricing increase, higher proportion of sales being completed under our leasing model, as well as increased throughput from our expanded production facility, where we have enhanced capacity and process automation.

Overall service revenue during the quarter increased 46% to $12.9 million, which is the strongest quarterly service growth achieved in three years. Software services were a major contributor to the growth, up 36% year-over-year, which also drove ARR growth of 38% to $42.4 million. Newly activated devices contributed to year-over-year growth of $1.5 million in the quarter, and net service increases within our existing customer base contributed $1.6 million of the growth. Our rental business also continues to generate robust growth, with revenue increasing 247% from the prior year to $1.6 million, meaning we have averaged over $1 million in quarterly rental revenue over the past four quarters.

Our service gross margin percentage came in at a record 75%, achieving our target set at the beginning of the year, two quarters ahead of schedule. Similar to product gross margins, we expect continued margin improvements through fiscal 2023, as we add new customers and renew existing customers under the new pricing model.

Our total gross margin percentage came in at 52%, yielding $12.5 million, representing our highest-ever total gross margin. The growth in total gross margin is due to revenue mix, cost optimization efforts across our business, and the rollout of our pricing increase.

In terms of our geographic growth mix, we are pleased with our performance, as each one of our key geographic markets improved from the year-ago comparable period. Our rest of world market represented our largest growth region, improving 123% from last year's Q2, as our sales team continues to deliver on the investments made over the past two years. The U.S. was our second largest growth market, at 65% from the year-ago comparable period, as we leveraged our established sales network in the region. Additionally, our Canadian and European markets were able to see a year-over-year increase of 24% and 17% respectively, as we continued to have excellent product wins and strong renewals across these regions.

Shifting now to operating expenses, our total expenses for the quarter were $19.2 million, which was down 11% compared to our expenses of $21.5 million in the prior year quarter. Excluding non-recurring transaction costs incurred in the quarter, total expenses as a percentage of revenue were 75% in the quarter, compared to 127% in the prior year period. It was our fourth consecutive quarter where we reduced our total expenses as a percentage of revenue.

Product research and development costs decreased 20% from the prior year quarter to $5.1 million, and decreased as a percentage of revenue to 21% from 38% in the prior year period. Salaries, recruitment expenses, and consulting and contractor costs associated with the G6 were all down, with the core development work of that product having been completed.

Sales and marketing expenses decreased 4% from the prior year quarter to $8.6 million, which represented 36% of revenue compared to 54% in the prior year period. Excluding a general provision for bad debts, sales and marketing expenses were 34% of revenue or an 8% decrease year-over-year. The decrease was a result of lower headcount and contractor expenses compared to the prior year. I would like to underscore that, even with this decrease, these go to market teams were key to driving revenue growth of 45% for the quarter.

General and administrative expenses increased 9% from the prior year quarter to $6.8 million, which represented 28% of revenue compared to 37% in the prior year. Excluding non-recurring transaction costs for our lease securitization facility and costs related to the departure of our Chief

Technology Officer, G&A was down 9% year-over-year and was 24% of revenue. This decrease was a result of reduced professional fees and subscription and license costs resulting from our cost reduction initiatives over the past year.

Moving on to capital expenditures, these totalled $2.8 million for the quarter, primarily for additions of revenue-generating sensor cartridges being used by customers and rental equipment to support the continued growth of that service line.

Inventory totalled $18 million at quarter end, compared to $18.7 million at the end of the fourth quarter. Recall that we had built up our inventory during fiscal 2022 for G6, G7, G7 Exo, due to global supply chain challenges, and have begun reducing inventory levels in the current quarter, as we fulfil our pipeline of orders and optimize our fulfilment strategy. Ultimately, this will allow us to improve our inventory turnover in the coming quarters, making it a source of cash for us over the balance of fiscal 2023.

Our G7 lease program has a total of $39.2 million in future contracted cash flow as of April 30, 2023, up from $36 million at October 31, 2022.

During the quarter, we closed our lease securitization facility with CWB Maxium and received initial funding of $8.3 million from the sale of the initial tranche of lease contracts. We will receive cash from our strong Q2 lease sales in our third fiscal quarter, with future funds being received approximately one month following the lease sale. With a $15 million CAD facility and a $35 million USD facility, we have plenty of capacity to grow our leasing program, which can potentially become the core of our go to market strategy, driving stronger margins and even better customer retention while lowering our overall cost of capital. We are pleased to have a financial partner like CWB Maxium, who is committed to the success of Canadian companies looking to grow beyond our home market.

At quarter end, we had total cash and short-term investments on hand of $21.9 million, $8 million of availability on our senior secured operating facility with ATB Financial, and $50 million CAD equivalent of availability under the lease securitization facility with CWB Maxium. The lease securitization facility will create a step change in our cash burn, which, combined with our improving gross margins and cost discipline, ensures the Company has the cash it requires to execute on our path to quarterly positive Adjusted EBITDA.

I will hand it back to Cody to discuss our outlook and to provide closing remarks. Cody?

**Cody Slater:**
Thank you Shane.

In closing, we are reiterating our goal to achieve positive quarterly Adjusted EBITDA by the end of this fiscal year, and remain firm in our belief that our high-margin recurring service revenue is key to delivering long-term profitability. Strengthening margins, corporate-wide cost discipline, $42 million in ARR, 118% net dollar retention, and increasing market adoption of our products by companies around the globe, we are well on our way to being a significantly profitable company.

I want to thank your customers for their continued trust in Blackline to help protect their most important and irreplaceable assets: their people. I also want to thank Blackline's own people around the world for their hard work, creativity, and their commitment to our purpose to ensure that every worker has the confidence to get the job done and return home safe, as we pursue our vision to transform enterprise workplaces through connected safety technology.

Thank you for your attention this morning, I'll now turn it over to the Operator for questions.

**Operator:**
Thank you. (Operator Instructions)

The first question comes from Doug Taylor with Canaccord Genuity. Please go ahead.

**Doug Taylor:**
Hi. Thanks, good morning, and congrats on a great growth performance this quarter.

Let me start by asking about the securitization facility that you announced sort of towards the end of this quarter. We can certainly see the impact it's having on the balance sheet in the near term. Is it too soon to say how or see the impact it's having on the sales velocity and your ability to secure new leased business? Is that still on the come here?

**Cody Slater:**

I'd say yes, that's still on the go now. That's still on—something you'd see in the future, Doug. Now that we've got securitization in place, we're shipping some of our marketing, some of the more making that whole program more visible with sort of X dollars per month kind of approach to the whole package of device and software, so I think you'd see that ramp up over time.

**Doug Taylor:**

Okay.

Let me switch gears and talk about, you know, the G6 rollout, you mention you expect to be on track with prior targets by Q4. I mean, last quarter you updated your expectations for units to be shipped this fiscal year, I think the last number was 25,000 to 30,000 units. Are you providing any update to that number today? Can you talk about what you've shipped so far?

**Cody Slater:**

I really just look at it, Doug, as saying it's similar number but rolling over between Q4 and Q1, kind of thing. What we really see in there, that we talk a bit about on the call is the G6 when it's launched was launched is really within that the core safety element on the zero maintenance side, but with a roadmap of a bunch of additional value-add data that would allow companies to have better visibility, deeper depth of data on work force, on site aspects. What we've really seen is that the customer base we're dealing with, a lot of whom know the G7, really want that extra value service, and that's really rolling out towards the end of our Q3 here, beginning of Q4.

From my view and the Company's view, what I'd say is the G6's, the market acceptance is exactly what we would have liked, even more so on some of the higher value base, because some of those services we're talking about, particularly the ones that get you closer to the kind of real-time work flow that you see from a G7 are, additional value adds, and extremely high-margin value adds for us.

So, no specific number for Q4, but if you look at Q4 and Q1, similar numbers to what we were talking about before.

**Doug Taylor:**

Okay, and so, I mean the combination of still expected benefits from G6, contributions to revenue in Q4 or Q1, and the benefits of securitization on the revenue and the income statement, your ability to sell that type of a pricing plan or model, and then with the pricing, I guess my question is, I mean should we be expecting, even from the 45% growth that you delivered here in Q2, growth to inflect higher through the balance of the year, and into next year?

**Cody Slater:**

Keep in mind our Q4 is always our strongest quarter, so if you're looking at it sequentially, you're going to see strong sequential growth, for sure, from Q2 to Q3, to Q3 through to Q4, and we're looking again at seeing very strong growth year-over-year in those actual numbers as well too. We wouldn't say that—again, keep in mind, Q4 always that top level quarter for us, as far as the hardware numbers, particularly the service will just continue that strong growth you've seen; the ARR growth will continue along the same sort of a path, not have a big inflection in the quarter at the year end, but good strong pickups, quarter on quarter, on hardware.

**Doug Taylor:**

Okay, I'll pass the line. Thank you.

**Cody Slater:**

Thanks Doug.

**Operator:**

The next question comes from Martin Toner with ATB Capital Markets. Please go ahead.

**Martin Toner:**

Thanks so much and congrats on a nice quarter, gentlemen.

Quick question on the—it just would be great if you guys could give us a little colour on some of the supply issues that are delaying the ability to ship G6.

**Cody Slater:**

It's not really supply issues, it's feature sets that were part of our long-term or mid-term roadmap on the G6. So, trying to say before, we launched the G6, it's competing in that zero maintenance market space, which is purely a safety product. If there's a problem, it beeps and flashes, the G6 has the connected value, it has the ability to actually create a rescue, do all those kinds of things, but when we had a roadmap that we're giving customers a greater depth of value around the data they could gather from the G6 itself, and what we're seeing is that customers want to see that in place prior to doing the ship. They perceive the value that we thought they would on that space, and really are willing to pay for that in the long run as well too.

It's not really a supply chain element on the G6, we've got inventory, we're ready to start shipping on the G6 right away, but it's more an element of delivering on that roadmap for some of the additional call them software services that were tied in with the G6.

**Martin Toner:**
Got you, okay, super. Thanks so much.

Any issues with the availability coinciding with Q1? I mean, given that that's the smallest sequential quarter, are you going to be able to get as much proverbial bang for your buck as you would in other quarters? Or, would you sort of temper our expectations there?

**Cody Slater:**
If we're talking about just the G6 itself, then we're going to look for a strong quarter in Q1, Q1 always has a drop-off as an overall base, so I'd still assume you're going to see that, but from Q4 to Q1, with a significant impact from the G6 in that, relating to, which will be in Q4 as well too.

**Martin Toner:**
Great. NRRs was particularly strong? Can you talk a little bit to some of the drivers of strength there?

**Cody Slater:**
On the ARR side?

**Martin Toner:**
No, sorry, NRR.

**Cody Slater:**

For the net dollar retention it's a series of different elements, it's really the selling of additional services, we're seeing the team there that's responsible for up-valuing the different services the customers have, the beginning of impact of that pricing increase, pricing change, it's portions of all those kinds of elements. Again it's that extreme—the other point I'd make is that we're still seeing really 100% retention basically, like we just don't see losses. A customer base, at that net dollar retention, was really strong pickup, again based on additional service sell, and based on the beginning of seeing that 15% price increase start to flow through our service channels—service renewals I should say.

**Martin Toner:**

Fantastic. Thanks so much, I'll pass the line.

**Operator:**

The next question comes from David Kwan with TD Securities. Please go ahead.

**David Kwan:**

Hey guys.

You guys have done a great job on reigning in the costs here to try to get to positive EBITDA. I guess, looking out, I guess at what point would you feel comfortable starting to ramp up some of these investments, as it relates to growth, sales and marketing, R&D and the like. Because obviously you've got a big opportunity out there, especially I think on the G6 side; but even on the G7 side there's lots of opportunity to penetrate more, obviously, customer—there are competitor displacements and whatnot, but just trying to want to understand how you're looking at the business from that standpoint.

**Cody Slater:**

The way we look at it is really that there's a lot of opportunity. One of our like our focus in this year has been what we call Into the Black, then next year a lot of our focus that is really on looking at optimization at some of our operations, services etc., there's a lot of opportunity to increase the scalability by investing in better systems for our order entry systems, our payable systems etc. So, from the overall outside cost standpoint, that will actually be able to drive those costs down as a percentage of revenue, long term, because we'll need less people to—given the increased volume of work we won't need to be adding people to do that, we'll be adding improvements to different technologies and services we're using internally. So, we look at really still a very strong cost base focus going forward into the next year, to allow us—but really focused on investing and allowing us to be a more scalable company across those aspects, which will make us, longer term, more profitable.

**David Kwan:**
So, would it be fair to say then, Cody, that, I guess, the gains that you might—the financial gains that you would get from this cost optimization activity would be kind of reinvested in for growth such as kind of the costs line, the OpEx line, should remain relatively flat?

**Cody Slater:**
Yes, I mean there'll be some growth in some aspects of it, but yes, for sure. Compared to revenue growth, for sure. Much, much lower element on the costs base.

**David Kwan:**
Okay, that's good to know.

On the gross margin side, you made some good gains there. I know I see you've had some headwinds on the product side, particularly as it relates to the supply chain. You're benefitting from the price increases and mix.

I guess, where now do you think the margins could get to? You've hit your target for the year on the services side. We've seen a nice sharp rebound on the products side. Like how should we be looking at that?

**Cody Slater:**
Really it would look at, you know, on the products side, there's still, you know, supply chain's obviously more of a challenge always on hardware than it is on the services side, still see the Company trending into 35% to 40% by the year end here. Probably now a little bit closer to that 35% than the 40% we've said before.

**David Kwan:**

How about on the services side? Like you're at 75%, that was kind of the target exiting the year. Like could we see much more improvement beyond that?

**Cody Slater:**

The service is a big number there. Yes, you'll see a little bit of improvement, a couple percentage points of improvement over the period of time. Again, we'll have more customers flowing through onto the higher-priced newer plans, and the new customers come in at that higher price as well too, which sort of helps drive that margin up a little bit.

**David Kwan:**

That's helpful. Last question. Can you talk maybe what you guys are getting on the generative AI front, I guess particularly as it relates to Blackline Analytics? I know, I think that's been a key differentiator for you guys.

Also, you've had a massive data advantage versus your peers, given that the G7's been on the market for many years longer than some that at least have a comparable product on the market. But do you think also genAI can help narrow that data gap?

**Cody Slater:**

I'd say what we're doing on that right now is more exploratory work, and not just in the data science side but in some of the other aspects of the design, development, customer support, those kinds of thing. So, it's definitely going to be something that will have a long-term impact for us, and you're right, the only way that becomes valuable is if you have the data, actually get those insights out of, and we are the only company out there that has that scale of that kind of customer-focus data. But right now I'd describe the work we're doing as exploratory.

**David Kwan:**

Appreciate the colour. Thanks.

**Cody Slater:**

Thanks.

**Operator:**

The next question comes from John Shao with National Bank. Please go ahead.

**John Shao:**

Hey good morning guys, thanks for taking my questions.

So, looks like the price increase has been fully rolled out among your customers, so could you share with us any customer feedback so far, and do you see any pushbacks or contract losses for that reason?

**Cody Slater:**

No pushbacks. No, I wouldn't say so, not that I'm seeing.

**John Shao:**

Okay.

It seems like the rental revenue has become a meaningful contributor of your total services revenue, so my question is, how should we think about the margin profile of that business? You mentioned it high margin, but is this comparable to the rest of the service business?

**Shane Grennan:**

Good morning, John. Yes, in general maybe a touch lower, given some of the other activities that are involved in the rental business, but a point between where the product margin is at and the service margin is at would be a good benchmark there, in terms of the rental revenues.

**John Shao:**

Thank you. I guess a related question on that topic is, so how much operating leverage does the rental business have as they continue grow was to from $1.6 million to potential of $3 million, $5 million in the near future, do you think that there's the potential that gross margin is going to fully scale?

**Shane Grennan:**

Within that base yes, for sure, John, as that business grows and there's less inputs needed in terms of building that business, that would be the expectation for sure.

**John Shao:**
Okay, thank you. My last question is, I just want to dig into the international market, especially the Middle East area. So, what kind of market dynamics does that region have, and, in terms of your presence in that market, so what would the Blackline Safety do to tap into the market potential in that region?

**Cody Slater:**
Sure, that's an interesting question. We really started investing in there a little over two years ago. The Middle Eastern market's an excellent market for us, we're really just starting to see the traction there now, so it's one where you need to have the feet on the ground, the people who know the marketplace, we do that very well. It's a long-term relationship, it's a bit longer-term introductions basically in that market, like customers want to get to—customers are large and they want to understand their suppliers well, so it's a longer of a ramp-up into some of the aspects there, but that's what we're starting to see that inflection point now in that market space, where you're going to see a strong pickup over the next four quarters, shall we say, as we start penetrating that market more. There's also, there's lots of different things you could talk about as far as different regulations, different other approvals you need for that market; we've got all that in place now, and now it's really a matter of starting to see the traction we can generate there.

**John Shao:**
Thank you, I'll pass the line.

**Operator:**
The next question comes from Jason Zandberg with PI Financial. Please go ahead.

**Jason Zandberg:**
Hey guys, thanks for taking my questions.

I just wanted to drill down a little bit more on the rental side. You'd mentioned that you'd invested in your rental equipment, in your CapEx this quarter. Just want to sort of get—if you could share sort of what you would expect to invest in that rental fleet for the remainder of the year, and sort of what's your expectation in terms of where this business can compete in this year or next year, in the near term?

**Cody Slater:**

I mean, over the next six months we're looking at putting another about a half million dollars in capital into the rental pool to allow for the growth in the rental space, we tend to—rental team does a superb job of their utilization that tends to run in the high 80's, so growth requires more investment in hardware into the space. Look at it over the next couple of quarters as being about a half a million dollars of investment there.

**Jason Zandberg:**

Okay. No, that's helpful. Then, you also mentioned that a lot of your customers, your rental fleet, one of the side benefits of that is, those rental contracts tend to convert into sales. Just wondering if you have any metrics to that in terms of how many customers actually do go into a long-term sales agreement after they do a rental agreement.

**Cody Slater:**

We have no direct metrics we can share with that, Jason, but I'd say it's introduced us to a number of new logos, like it's added logos to our customer base, to a reasonably significant degree. But we don't actually have a specific number that we've tracked that says this is the relationship one to the other. Like I said, the biggest thing for us is getting into a customer in what I would say is off cycle, so if you've got a customer who is normally buying their gas detection every four or five years and it's maybe two-three years out but they're doing a turnaround or a construction opportunity, you get in there with our product that gives them an opportunity to see what we can do, the value of the connected services, and it is a significant opportunity to lead to sales. But again I'd just say, the point I'd make is that it has actually already added new logos to the customer base here.

**Jason Zandberg:**

Okay. Great, thanks very much.

**Operator:**

The next question comes from Raj Sharma with B Riley. Please go ahead.

**Raj Sharma:**

Thank you for taking my questions. Congratulations on solid results.

Can you please remind me, refresh, the G6 delay in Q3 is only related to feature sets, not any supply chain issues, or …

**Cody Slater:**
Yes. That's correct. It's just really it's been customers looking at the product, asking for—once they see something connected now, given what we've done with the G7, they know themselves what other values they'd like. Fortunately everything they've been asking for is something that's been on our roadmap, so it's something we've been anticipating delivering, but delivering in that Q4 period. So, once we're over that development hump there, then there'll be no restriction on us shipping product.

**Raj Sharma:**
Got it. Thank you. Then, the lease contracts, they are about—so, the rental income in the lease contracts and that's about little over 12%, 13% of product sales, every quarter?

**Shane Grennan:**
I would just say that there are two distinct business activities happening here, Raj, the rental are under discrete rental agreements with various organizations, and the lease agreements themselves are—the product-associated revenue is captured within our product revenues.

**Cody Slater:**
Our typical number as a percent—sorry, Raj, I was just going to add that the percentage of our sales that tend to be in lease, right around, I would say, 25% to 30% …

**Raj Sharma:**
Oh great.

**Cody Slater:**
… of the hardware

**Raj Sharma:**
Of product revenues.

**Cody Slater:**

Correct, yes. Yes. Correct.

**Raj Sharma:**

Do you see that percentage going up in the next few months, in the next 12 months?

**Cody Slater:**

The next 12 months, yes. Next few months, no, I don't think we'll—like it won't be like turning on a switch, but it's a nice way, from a company's standpoint, it's a nice system, it's $50 a month, it's simple, it's clean, it includes everything. From our standpoint in the past, it was just a very negative impact on cash flow. With the securitization with CWB Maxium, now it's almost the opposite, the payment terms are pretty quick and direct, and so it's an easier thing for us to press a little bit more. We do believe the market is very receptive to that as—so, a higher percentage down the long term of companies will likely take advantage of that.

**Raj Sharma:**

Got it. So, I just wanted, I guess, to get a understanding of, over the next 12 months, the percentage of product that would be leased, and also what securitization cash flow could you expect?

**Cody Slater:**

Still, we're looking at …

**Raj Sharma:**

Or, is it tough to tell?

**Cody Slater:**

As I say, I think we can do better than the 25% we've been doing, but it's a number we don't drive, it's a number the customer does, at the end of the day, dependent on markets, it's dependent on other things. Given, one thing we'll say with this CWB line is that the line has capacity to handle what we're looking at doing for leasing for the next couple of years.

**Raj Sharma:**

Right. The total $15 million, about, 15 plus 35 …

**Cody Slater:**

Yes.

**Raj Sharma:**

Right. Then lastly, just could you comment on the CapEx? Was it a CapEx requirement or any CapEx spent on the new capacity expansion at your headquarters?

**Shane Grennan:**

No, Raj, there hasn't been extensive expenditures incurred in relation to that. We captured most of that in the fourth quarter of last year, there may be a small element that you'll see coming forward into the third quarter, but you're not going to see extensive spending happening in the third quarter for that.

**Raj Sharma:**

Right. Do you think that the capacity expansion takes care of the growth for the next few years, at this pace?

**Cody Slater:**

I wouldn't necessarily say, you know, it's something we'll always be looking at investing in. That certainly gives us the capacity to do what we'd like to be doing for the next year or so. Dependent then on how the growth is looking at, we'll look at that on an ongoing basis as to when do we invest more into that.

**Raj Sharma:**

Got it. Yes, that's all for me, and thank you so much for answering my questions.

**Cody Slater:**

Thanks Raj.

**Raj Sharma:**

Congratulations again.

**Cody Slater:**

Thank you.

**Raj Sharma:**

Thanks.

**Operator:**

This concludes the question and answer session. I would like to turn the conference back over to Cody Slater for any closing remarks. Please go ahead.

**Cody Slater:**

Just want to thank you all for attending the call, and we'll wish you a good rest of the day. Thank you very much.

**Operator:**

This concludes today's Conference Call. You may disconnect your lines. Thank you for participating, and have a pleasant day.