



Fortinet Q1 2025 Earnings Prepared Remarks

Aaron Ovadia, Senior Director, Investor Relations

Thank you and good afternoon everyone. This is Aaron Ovadia, Senior Director of Investor Relations at Fortinet. I am pleased to welcome everyone to our call to discuss Fortinet's financial results for the first quarter of 2025.

Joining me on today's call are Ken Xie, Fortinet's Founder, Chairman, and CEO, Keith Jensen, our CFO, Christiane Ohlgart, our CAO and Sales Operations Leader, and John Whittle, our COO. As a reminder, Keith will be stepping down from the CFO role on May 15th and Christiane will take over as our next CFO.

Ken will begin our call today by providing a high-level perspective on our business. Keith will then review our financial results for the first quarter of 2025 and Christiane will provide a forward-looking view, including guidance for the second quarter and updating the full year. We will then open the call for questions.

During the Q&A session, we ask that you please limit yourself to one question and one follow up question to allow others to participate.

Before we begin, I'd like to remind everyone that on today's call we will be making forward-looking statements and these forward-looking statements are subject to risks and uncertainties which could cause actual results to differ materially from those projected.

Please refer to our SEC filings, in particular the risk factors in our most recent Form 10-K and Form 10-Q, for more information.

All forward-looking statements reflect our opinions only as of the date of this presentation and we undertake no obligation, and specifically disclaim any obligation, to update forward-looking statements.

Also, all references to financial metrics that we make on today's call are non-GAAP, unless stated otherwise. Our GAAP results and GAAP to non-GAAP reconciliations are located in our earnings press release and in the presentation that accompany today's remarks, both of which are posted on our investor relations website.

As a reminder, this is a live call that will be available for replay via webcast on our investor relations website. The prepared remarks will also be posted on the Quarterly Earnings section of our investor relations website following today's call.

Lastly, all references to growth are on a year-over-year basis, unless noted otherwise.

I will now turn the call over to Ken.

Ken Xie, Founder, Chairman and CEO

Thank you, Aaron, and thank you to everyone for joining our call.

We are pleased with our strong performance in the first quarter, successfully balancing growth and profitability, including:

- Billings and revenue growth of 14%,
- Record first quarter operating margin of 34%,
- Record free cash flow of \$783 million - a margin of 51%,
- And strong growth in Security Operations and Unified SASE with security service edge billings growth of over 110%, which drove our Unified SASE billings growth to 18%, accounting for 25% of our business.

Fortinet's leadership in innovation and long-term investment is evident in our market position as:

- The #1 deployed firewall vendor worldwide,
- A market leader in SD-WAN and OT Security,

- And with our strong SASE strategy and growth, we are confident we will be #1 in this space as well.

The strong momentum behind our Unified SASE pillar underscores the value customers place on our single OS platform. The typical SASE journey begins with a customer's initial purchase of Fortinet's industry-leading, ASIC-based FortiGate firewall, powered by FortiOS. From there, the majority of large enterprise customers expand into SD-WAN before progressing into our FortiSASE solution. This expansion path continues to grow, as 73% of our larger enterprise customers have now adopted our SD-WAN solution and have either begun or are well-positioned to transition to FortiSASE, with our FortiSASE penetration among large enterprises increasing nearly 10% quarter over quarter to 11%.

We remain the only vendor to have organically developed all of the core SASE capabilities within a single operating system, FortiOS, including Next-Gen Firewall, SD-WAN, ZTNA, Secure Web Gateway, CASB, and DLP technologies. This native integration of networking and security reduces complexity and operating costs while enhancing user experience and ensuring secure across both on-premises and cloud environments.

In addition to our traditional SASE offering, we also offer Sovereign SASE, a tailored solution for large enterprises and service providers that require full on-premises or in-country control of their data. With Sovereign SASE, customers can deploy FortiSASE within their own data centers, ensuring that all data is processed exclusively through customer-owned or country-specific locations to meet compliance requirements by countries or industry regulations. This approach accelerates performance through our FortiASIC technology, and is well-suited for highly regulated sectors such as finance, government, and healthcare.

AI-driven Security Operations billings increased by 29%, accounting for 10% of our business, as customers continue to consolidate multiple security vendors on our integrated and AI-enhanced FortiFabric solution.

Looking ahead, in addition to SASE and SecOps, we expect OT Security and AI to be key growth drivers over the next 5 years.

In OT Security, a rapidly expanding market driven by a surge in connected devices, Fortinet is recognized as the only leader in the Westlands Advisory Report, supported by over a decade of strategic investment and specialized solutions positioning us for continued growth.

We also continue to invest in our AI capabilities, which we began developing more than 15 years ago, and now hold over 500 issued and pending AI patents, more than any other competitor, with our AI technology now integrated into a dozen products. New AI capabilities like FortiAI-Assist for automating security tasks, FortiAI-Protect for advanced threat detection, and FortiAI-SecureAI for protecting AI infrastructure.

Today, we announced the FortiGate 700G series, a high-performance firewall for mid-sized businesses and distributed enterprises. Powered by our FortiASIC technology, which delivers a 5x to 10x performance advantage over competitors, and FortiOS, the only operating system recognized across five secure networking Gartner Magic Quadrants, this approach significantly lowers total cost of ownership and complexity, while reducing energy consumption, and drives Fortinet's continued strong growth and market share gains in Secure Networking.

I would like to thank our employees, customers, partners, and suppliers worldwide for their continued support and hard work. I'll now turn the call over to Keith and Christiane.

Keith Jensen, CFO

Thank you, Ken, thank you Aaron, welcome Christiane, and good afternoon everyone.

Let's start with the key financial highlights from the first quarter before handing the call off to Christiane for a more detailed forward-looking view...

We delivered strong performance and top-line results that approached the high-end of our guidance range, together with *record* first quarter operating margin of 34%.

Total revenue grew 14%, driven by strong product and service revenues with product revenue growth of 12%.

In addition, new logos increased 14% to over 6,300, driven by continued worldwide investments in our channel partners.

Looking at our financial results in more detail...

Total billings grew 14% to \$1.6 billion, driven by 18% growth in Unified SASE and 29% growth in AI-driven SecOps. Unified SASE and SecOps now account for 25% and 10% of total billings, respectively, up 1 point each.

RPO grew 12% to \$6.5 billion, while current RPO grew over 15% to \$3.4 billion.

Unified SASE and SecOps ARR increased 26% and 30%, respectively, reaching a combined ARR of \$1.6 billion.

Turning to revenue and margins....

Total revenue grew 14% to \$1.54 billion.

Product revenue increased 12% to \$459 million, driven by growth in both hardware and software solutions.

FortiGate hardware revenue grew in the mid-teens, outpacing total product revenue growth, driven by strong performance in low-end and high-end models, and supported by early-mover, large enterprise customers upgrading their firewall infrastructure.

Software license revenue grew in the mid-teens and represented a high teens percentage of total product revenue, driven by on-prem, time-based software license growth of over 30%.

Service revenue of \$1.08 billion grew 14% to 70% of total revenue. Security subscriptions revenue increased 16%, while support and related service revenues

increased 12%. Service billings grew 14%, *our highest growth rate in the past 5 quarters.*

Total gross margin *increased 380 basis points to 81.9%* and exceeded the high end of the guidance range by 90 basis points.

Product gross margin of 67.7% increased *1,200 basis* points as inventory related charges normalized from the highly elevated levels we saw in the first half of 2024, this added approximately 1,300 basis points to product gross margin and approximately 400 basis points to total gross margin.

Service gross margin of 87.8% was down just 10 basis points, as we successfully absorbed increased costs associated with the expansion of hosted security solutions.

Operating margin *increased 570 basis points to a first quarter record* of 34.2% and was 320 basis points *above* the high-end of our guidance range, reflecting the strong gross margin, an Fx tailwind of around 100 basis points, and cost efficiencies in the business.

Looking to the Statement of Cash Flows summarized on slides 18 and 19...

Free cash flow tends to be seasonally strong in the first quarter and was a record of \$783 million, while free cash flow margin was 51%, up 6 points. Adjusted Free Cash Flow was \$839 million, representing a margin of 54%.

Infrastructure investments were \$67 million, down \$155 million due to a lower level of real estate investment.

Cash taxes were \$27 million.

The average contract term was 27 months, roughly flat year-over-year and down 2 months quarter-over-quarter.

And while we did not repurchase shares during the first quarter; we did repurchase approximately 4.6 million shares for a total of \$401 million during the month of

April. The remaining share buyback authorization as of today is approximately \$1.6 billion.

I will now turn the call over to Christiane to share a few significant wins from the first quarter as well as a more forward-looking view, including business conditions, and the second quarter and full year guidance.

Christiane Ohlgart, CAO

Thank you, Keith.

As Ken mentioned earlier, the noteworthy headline in this uncertain macroeconomic environment is that customer adoption of our solutions is accelerating. This momentum is driven by two key factors:

- One: our decades-long innovation leadership, and
- Two: our competitively-differentiated dedication to putting the customer-first.

Together, this creates a powerful network effect, with some of the most discerning organizations rapidly adopting Fortinet's solutions at scale. This is exemplified by Fortinet being the #1 solution in firewall as well as a leader in SD-WAN and OT Security. Also, our leading SASE strategy is driving strong growth, reinforcing our confidence in becoming the #1 player in the SASE market.

Building on this momentum, our SSE solution is gaining strong traction, fueled by continued success in upselling SSE to our large SD-WAN customer base. With both ARR and billings growth at over 100%, we believe FortiSASE is the fastest growing SSE solution at scale in the market.

As shown on slide 7, the typical FortiSASE journey begins with a customer purchasing our market-leading, FortiGate firewall, followed by an expansion to SD-WAN and then onto our single-vendor SASE solution. Our adoption of SD-WAN and SSE continues to grow, with our large enterprise expansion penetration

rates increasing to 73% and 11%, respectively, with the SSE penetration rate growth increasing nearly 10% quarter over quarter.

In addition, a second customer buying journey illustrates the growing convergence of security and networking – it too starts with our FortiGate firewalls and expands to our switches and access points. The key to this expansion is FortiOS' FortiLink technology, which enables seamless management of our switches and access points through our unified operating system. Our increased penetration rates show the success of this strategy.

Now, I'd like to review some deals that showcase our SASE adoption and customer expansion...

In an 8-figure displacement deal, an international government purchased our SD-WAN solution as well as our FortiSASE solution to secure their hybrid workforce of 6,000 users. This customer chose Fortinet for its ability to deliver flexible and consistent security enforcement, ensuring secure access to both on-premises and cloud applications while maintaining a seamless user experience. By harnessing the power of our FortiOS, we delivered superior performance over the competition, reduced total cost of ownership, and effectively consolidated multiple security functions into a single, integrated platform.

In another SASE win, we replaced the incumbent vendor at an international education provider, which chose FortiSASE for their 40,000 users. The decision to transition to FortiSASE was driven by ongoing performance challenges with their previous SASE vendor. Keys to this win included FortiSASE's ease of use, seamless integration with the Fortinet Security Fabric, and proven scalability across their SD-WAN sites. Based on the success from their proof-of-concept, this customer will benefit from improved performance, consistent security for users everywhere, and greater operational efficiency.

In a 7-figure deal, a large multinational manufacturing company selected our SD-WAN and multiple SecOps solutions. Fortinet displaced the legacy SD-WAN provider by demonstrating how FortiOS simplifies operations, reduces total cost of

ownership, and unifies security and networking functions on a single platform. The integrated nature of FortiOS also enables seamless alignment with the company's existing Fortinet security infrastructure, establishing a strong foundation for future projects.

Lastly, a Fortune 500 company signed an 8-figure deal that spans all three of our pillars. Over the past three years, they've expanded their FortiGate install base by more than 80%, driven by our world-class support for their data centers and branch locations, as well as the automation and seamless integration enabled by our FortiOS operating system.

Rounding out the billings commentary...

- Large enterprise was our top performing customer segment with growth of around 30%.
- The number of deals greater than \$1 million were up 30%, including three 8-figure deals this quarter, up from one during the same period last year.
- EMEA was our best performing geography, driven by mid-teens growth from International Emerging.
- Among our top 5 verticals, financial services and worldwide government led the way with growth of over 20%.

Before moving onto guidance, I'd like to spend a few minutes discussing the current U.S. tariff situation...

The U.S. tariff situation landscape is evolving rapidly, and our comments on this call reflect the information currently available to us.

Despite the current geopolitical uncertainties, demand for our cybersecurity solutions remains strong. Our pipeline continues to grow and we are not seeing signs of near-term erosion. Additionally, our close rates remain robust and sales cycles are tracking within our normal historical range.

For the second quarter, we do not expect U.S. tariffs to have a meaningful impact on our operating margin as only a few components are subject to tariff charges. Should tariffs increase in the future, we expect any resulting impact on our operating margin to be limited to hardware sales to U.S. customers. As long as our international hardware sales do not flow through the U.S., they are not subject to U.S. import tariffs.

Moving onto guidance...

As a reminder, our second quarter and full year outlooks, which are summarized on slides 21 and 22, are subject to the disclaimers regarding forward-looking information that Aaron provided at the beginning of the call.

While our business remains strong and we outperformed on the top line in the first quarter with continued confidence in our ability to execute, we recognize that our customers' investment decisions can be influenced by the broader economic outlook. As a result, we are maintaining our full year billings and revenue guidance ranges to account for potential top line risks associated with the evolving geopolitical environment.

Regarding the record firewall upgrade cycle that we've spoken about previously, we continue to expect the firewall upgrade cycle to gain momentum in both purchasing and planning activities in the second half of 2025.

Looking at the bottom line, the U.S. dollar weakened more than anticipated from early February when we first issued our 2025 guidance. As a result, we expect an operating margin headwind of approximately 120 basis points to the second quarter and approximately 90 basis points to the full year, which is factored into today's outlook. Despite the FX headwinds, we are raising the midpoint of our full year operating margin guidance as a result of our first quarter outperformance and expected efficiencies in the business.

Our continued business momentum and strong execution gives us confidence that we are on track to achieve the 'Rule of 45' for the 6th consecutive year.

For the second quarter, we expect:

- *Billings* in the range of \$1.685 billion to \$1.765 billion, which at the midpoint represents growth of 12%,
- Revenue in the range of \$1.590 billion to \$1.650 billion, which at the midpoint represents growth of 13%,
- Non-GAAP gross margin of 80.0% to 81.0%,
- Non-GAAP operating margin of 31.5% to 32.5%,
- Non-GAAP earnings per share of \$0.58 to \$0.60, which assumes a share count between 773 and 777 million,
- Infrastructure investments of \$180 to \$200 million.
- A non-GAAP tax rate of 18%, and
- Cash taxes of \$230 to \$255 million.

For the full year, we expect:

- *Billings* in the range of \$7.200 billion to \$7.400 billion, which at the midpoint represents growth of 12%,
- Revenue in the range of \$6.650 billion to \$6.850 billion, which at the midpoint represents growth of 13%,
- Service revenue in the range of \$4.575 billion to \$4.725 billion, which at the midpoint represents growth of 15%,
- Non-GAAP gross margin of 79.0% to 81.0%,
- Non-GAAP operating margin of 31.5% to 33.5%,
- Non-GAAP earnings per share of \$2.43 to \$2.49, which assumes a share count of between 769 and 779 million,
- Infrastructure investments of \$380 to \$430 million,

- Non-GAAP tax rate of 18%, and
- Cash taxes of between \$525 million and \$575 million.

I'll now hand the call back over to Aaron to begin the Q&A session.

Closing Remarks: Aaron Ovadia, Senior Director, Investor Relations

Thank you. I'd like to thank everyone for joining today's call.

We will be attending investor conferences hosted by J.P. Morgan and Bank of America during the second quarter. The fireside chat webcast links will be posted on the Events and Presentations section of our investor relations website.

If you have any follow-up questions, please feel free to contact me.

Have a great rest of your day!