



Investor Presentation

As of June 30, 2023

Safe Harbor



This presentation and the accompanying oral commentary have been prepared by Cloudflare, Inc. ("Cloudflare") for informational purposes only and not for any other purpose. Nothing contained in this presentation is, or should be construed as, a recommendation, promise, or representation by the presenter or Cloudflare or any officer, director, employee, agent, or advisor of Cloudflare. This presentation does not purport to be all-inclusive or to contain all of the information you may desire. Information provided in this presentation and the accompanying oral commentary speak only as of the date set forth on the cover page of this presentation.

This presentation and the accompanying oral commentary contain express and implied "forward-looking" statements within the meaning of the federal securities laws, and these statements involve substantial risks, assumptions, and uncertainties. All statements other than statements of historical fact could be deemed forward-looking, including, but not limited to, the current and planned development and functionality of our products, demand for our products, our ability to effectively sell our existing and new products, expectations of future operating results or financial performance, business strategy and plans, the impact of adverse macroeconomic conditions, such as inflation, changes in interest rates, actual or potential bank failures and recessionary concerns, the impact of the Russia-Ukraine conflict and other areas of geopolitical tension around the world, market volatility, size and growth opportunities, the calculation of certain of our key financial and operating metrics, capital expenditures, plans for future operations, competitive position, rapidly evolving technological developments, including advancements in AI, and strategic relationships, as well as assumptions relating to the foregoing. Forward-looking statements are inherently subject to risks and uncertainties, some of which cannot be predicted or quantified. In some cases, you can identify forward-looking statements by terminology such as "may," "will," "should," "could," "expect," "plan," "anticipate," "believe," "estimate," "predict," "intend," "potential," "would," "continue," "ongoing" or the negative of these terms or other comparable terminology. You should not put undue reliance on any forward-looking statements. Forward-looking statements should not be read as a guarantee of future performance or results and will not necessarily be accurate indications of the times at, or by, which such performance or results will be achieved, if at all.

Actual results could differ materially from our current expectations as a result of many factors, including those identified in the "Risk Factors" section of our filings made with the Securities and Exchange Commission ("SEC"). You can locate these reports on our investor relations website (<https://cloudflare.NET>) or on the SEC website (www.sec.gov). If the risks or uncertainties ever materialize or the assumptions prove incorrect, our results may differ materially from those expressed or implied by such forward-looking statements. Forward-looking statements included in this presentation represent our views only as of the date of this presentation, and except as required by law, we assume no obligation and do not intend to update these forward-looking statements or to conform these statements to actual results or to changes in our expectations.

In addition to our results determined in accordance with generally accepted accounting principles ("GAAP"), this presentation includes certain non-GAAP financial measures. These non-GAAP financial measures are in addition to, and not as a substitute for or superior to measures of financial performance prepared in accordance with U.S. GAAP. There are a number of limitations related to the use of these non-GAAP financial measures versus their nearest GAAP equivalents. For example, other companies may calculate non-GAAP financial 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. See the appendix for a reconciliation of those measures to the most directly comparable GAAP measures.

This presentation and the accompanying oral commentary may contain statistical data, estimates, and forecasts that are based on independent industry publications or other publicly available information, as well as other information based on our internal sources. This information involves many assumptions and limitations, and you are cautioned not to give undue weight to these estimates. We have not independently verified the accuracy or completeness of the data contained in these industry publications and other publicly available information. Accordingly, we make no representations as to the accuracy or completeness of that data nor do we undertake to update such data after the date of this presentation.

By attending or receiving this presentation you acknowledge that you will be solely responsible for your own assessment of the market and our market position and that you will conduct your own analysis and be solely responsible for forming your own view of the potential future performance of our business and products.

The trademarks included herein are the property of the owners thereof and are used for reference purposes only. Such use should not be construed as an endorsement of the network and products of Cloudflare.

Cloudflare at a Glance

2010

Launched

174K

Paying
Customers

300+

Cities in
Network

>60%

Of Revenue from
Large Customers

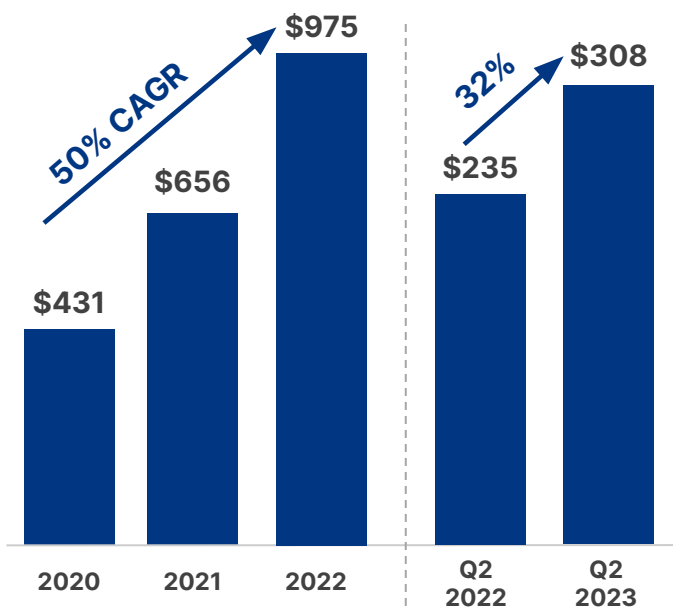
3,389

Employees

76%

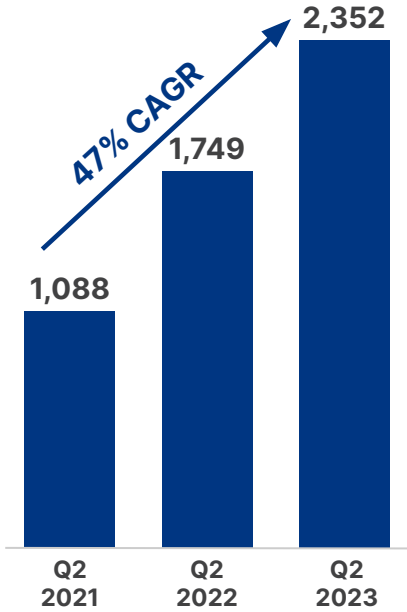
GAAP Gross
Margin

Total Revenue (\$M)



Large Customers

> \$100,000 Annualized Revenue



Note: Unless indicated otherwise, all data in orange shaded area of slide are as of June 30, 2023, except revenue from Large Customers and GAAP gross margin are for three months ended June 30, 2023. See Appendix for "Large Customers" definition.

Environmental, Social, Governance

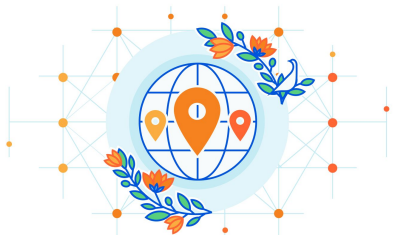


Building a Greener Internet

Recycling 95% of decommissioned data center hardware

70,000 Trees Donated

Coming Soon: Cloudflare vs. On-Prem Emissions Study



Human Rights and Democracy

Protecting more than 2,200 journalists and human rights defenders online in 111 countries for free through [Project Galileo](#)

[Protecting](#) state and local governments' election websites in 31 US States

Human rights due diligence audit (GNI)



Building Sustainable Communities

UN Global Compact Signatory

Diversity, Equity, Inclusion Report

Annual Impact Report/ESG Index (12/22)

1% Pledge Participant



Cloudflare is powered by 100% renewable energy and committed to offsetting or removing all of its historic network emissions by 2025.

Newsweek's 100 Most Loved Workplaces 2022 (#55)

Cloudflare recognized by the [White House](#) and State Department at 2023 Summit for Democracy

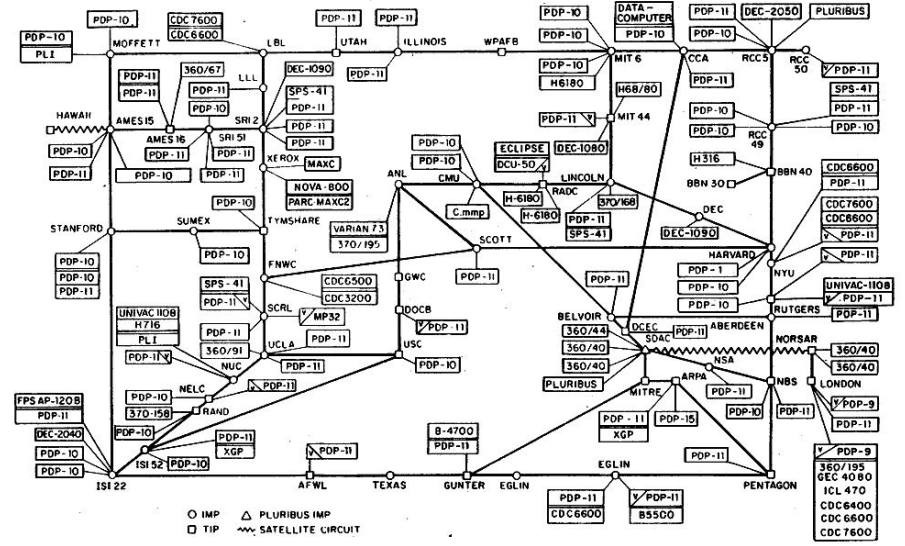
For more information, visit

<https://www.cloudflare.com/impact/>

Cloudflare's mission is to
Help build a better Internet

The Internet
was not
built for
what it has
become.

ARPANET LOGICAL MAP, MARCH 1977

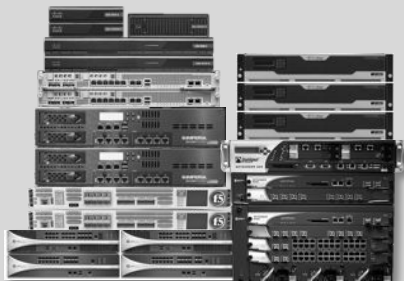


(PLEASE NOTE THAT WHILE THIS MAP SHOWS THE HOST POPULATION OF THE NETWORK ACCORDING TO THE BEST INFORMATION OBTAINABLE, NO CLAIM CAN BE MADE FOR ITS ACCURACY)
NAMES SHOWN ARE IMP NAMES, NOT NECESSARILY HOST NAMES

From Endless Hardware to a Global Cloud Platform

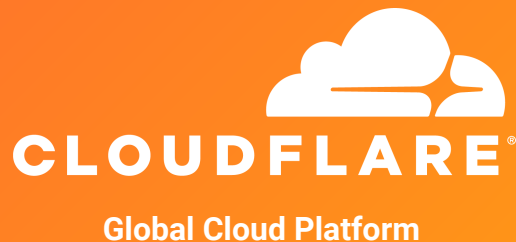
BAND-AID BOXES

- Costly and complex
- Web of dependencies
- Specialized hardware
- On-premise only
- Point solutions

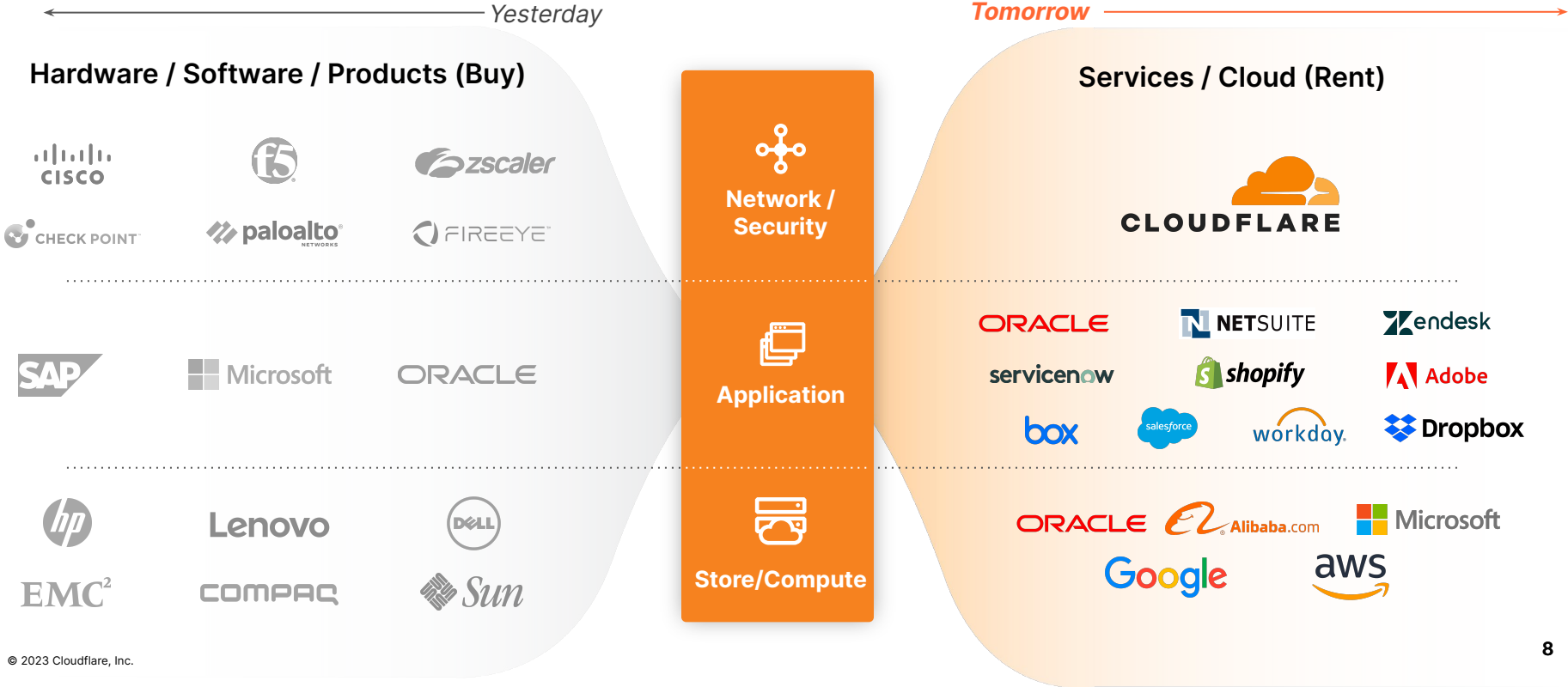


BETTER INTERNET

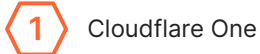
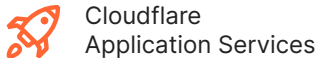
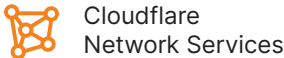
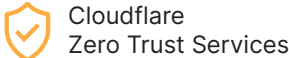
- Easy-to-use, flexible, and scalable
- Unified control plane
- Serverless cloud architecture
- Cloud, hybrid, on-premise, and SaaS
- Broad, integrated product platform



Evolution of the Enterprise Stack



An Integrated Global Cloud Platform



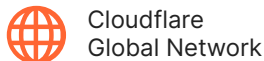
- Zero Trust Network Access
- Secure Web Gateway
- Cloud Access Security Broker
- Cloud Email Security
- Remote Browser Isolation
- Data Loss Prevention

- WAN-as-a-Service
- Firewall-as-a-Service
- L3 & L4 DDoS Protection
- Network Interconnect
- Smart Routing
- IDS/IPS

- WAF with API Protection
- Rate Limiting
- Load Balancing
- Bot Management
- L7 DDoS Protection
- CDN and DNS



- Workers
- Pages
- R2
- Workers KV
- Durable Objects
- Images
- Stream

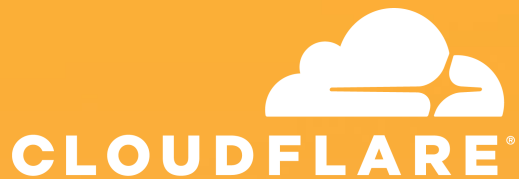


- Compliance/Privacy:** FedRAMP, ISO, SOC, PCI, GDPR compliant, Logs & Analytics, Data Localization Suite

We Operate at Massive Scale



Cyber threats blocked per day is average over the three months ended June 30, 2023. All other figures are as of the three months ended June 30, 2023. See Appendix for "Paying Customers" and "Large Customers" definitions.
© 2023 Cloudflare, Inc.



Our Flexible, Scalable, & Efficient Serverless Architecture

- Abstracts underlying infrastructure
- Dynamically optimizes and leverages capacity across network
- Single unified code base
- Deployment on commodity hardware

A Global Network Powering our Platform



300+ cities

in 100+ countries, including mainland China



12,500 networks

directly connect to Cloudflare, including ISPs, cloud providers, and large enterprises

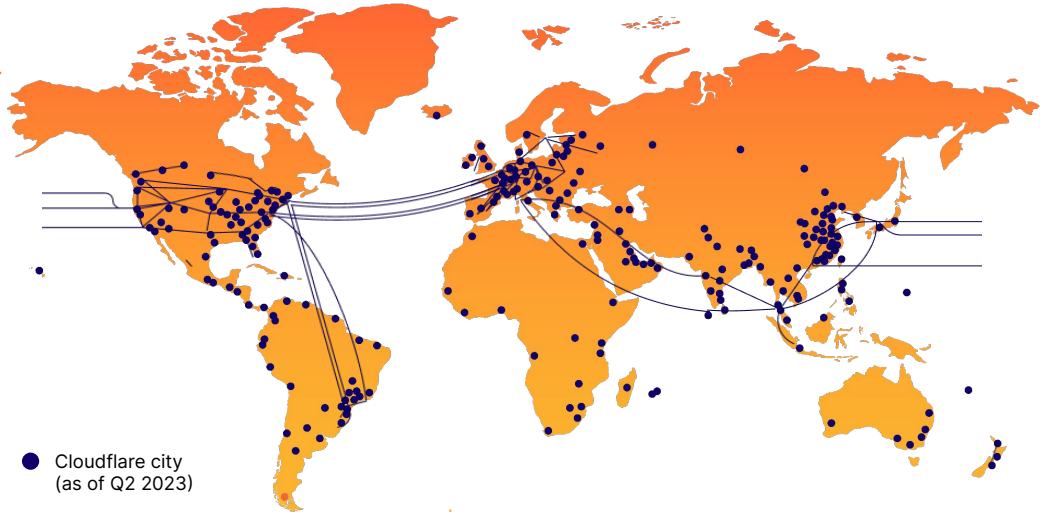


209 Tbps

of network capacity and growing



174,000+ Paying Customers



~31%

of the Fortune 1,000 are Paying Customers
as of June 30, 2023

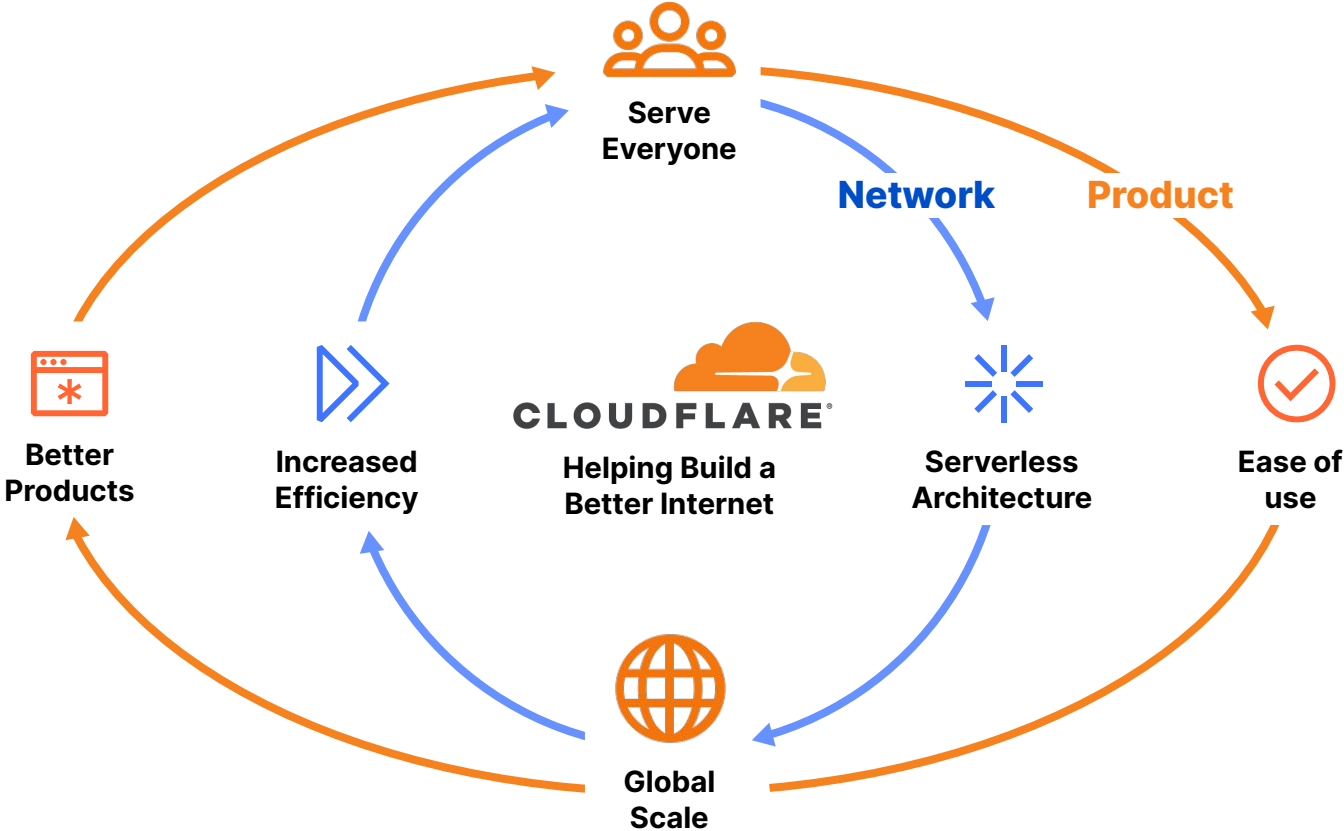
34%

year-over-year Large Customer growth in Q2'23

~95%

of the world's population is within ~50 ms of a
Cloudflare data center

Our Product & Network Flywheels Drive Our Business



Data Intelligence & Quality Assurance at Scale

Global sensor network

with paying customers in 180+ countries.

Machine learning systems
improve products with
every customer's request.

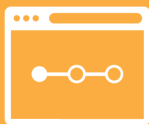
Immune system for the
Internet blocking an average of
140 billion cyber threats each day.

Rapid development cycles
and QA through free users
volunteering to test new products.

Our Competitive Advantages



**NETWORK
SCALE**



**EASE
OF USE**












**SHARED
INTELLIGENCE**



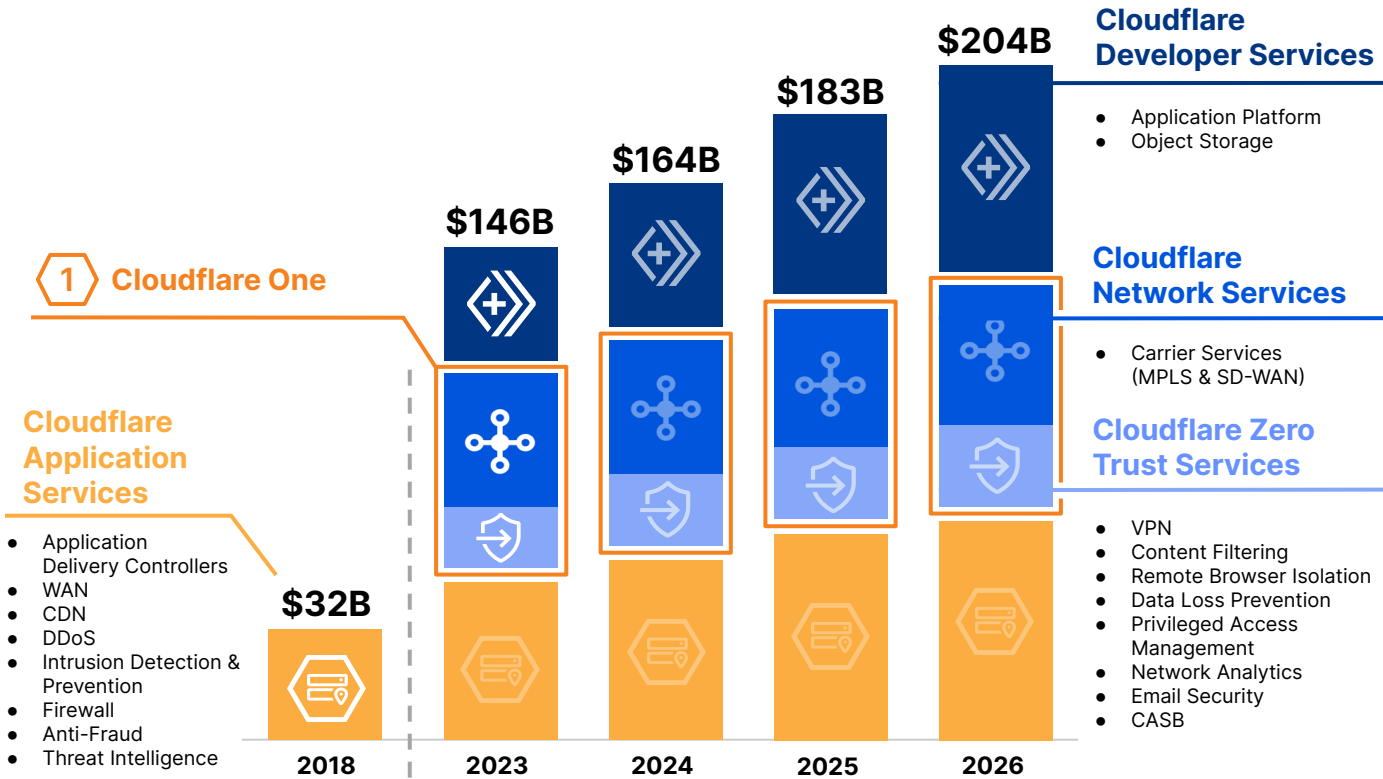
**NO
TRADE OFFS**

Our Favorable Competitive Position

Limitations

 <p>On-Premises</p>	 	<ul style="list-style-type: none">• Complex and expensive• Not suited to address cloud-based and hybrid deployments
 <p>Point Solutions</p>	 	<ul style="list-style-type: none">• Architected to deliver single point / more narrow product portfolio• Customers are increasingly looking for an integrated platform offering security, performance, and reliability through a single vendor
 <p>Public Cloud</p>	 	<ul style="list-style-type: none">• Inability to serve as a unified control plane across on-premise, cloud, hybrid, and SaaS infrastructure• Customer lock-in and competition concerns

Consistent & Deliberate TAM Expansion



Areas for Potential Incremental Growth

- AI
- Database
- Internet of Things
- 5G Cellular
- Network Services

Note: Total Addressable Market figures are Cloudflare estimates based on IDC market forecasts. Figures reflect the markets addressed by our current product offerings. For markets not profiled by IDC forecasts, such as threat intelligence software and anti-fraud software, Cloudflare's estimates are based on Gartner, Inc., Forecast: Information Security and Risk Management, Worldwide, 2021-2027, 1Q23 Update, Shailendra Upadhyay, Rahul Yadav, et.al., 03/29/2023.

Traditional Go-To-Market Model Inverted

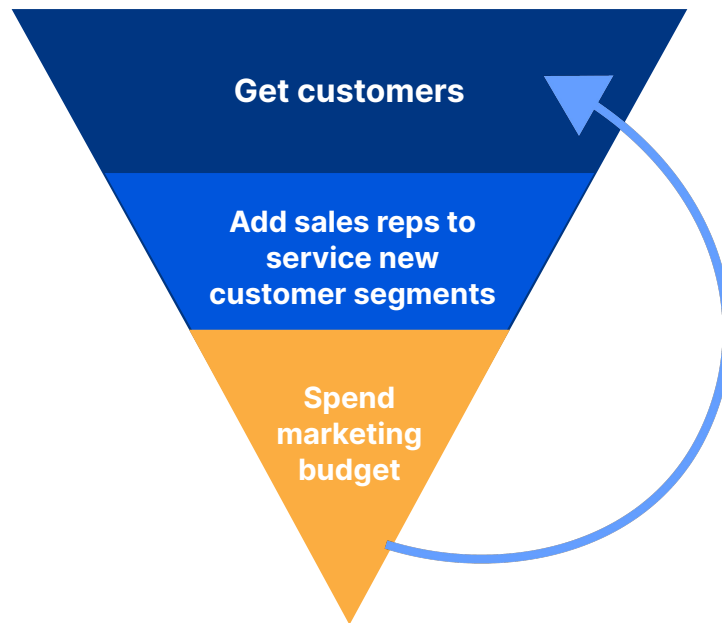
We don't build ahead of the curve.

Sources of Leverage

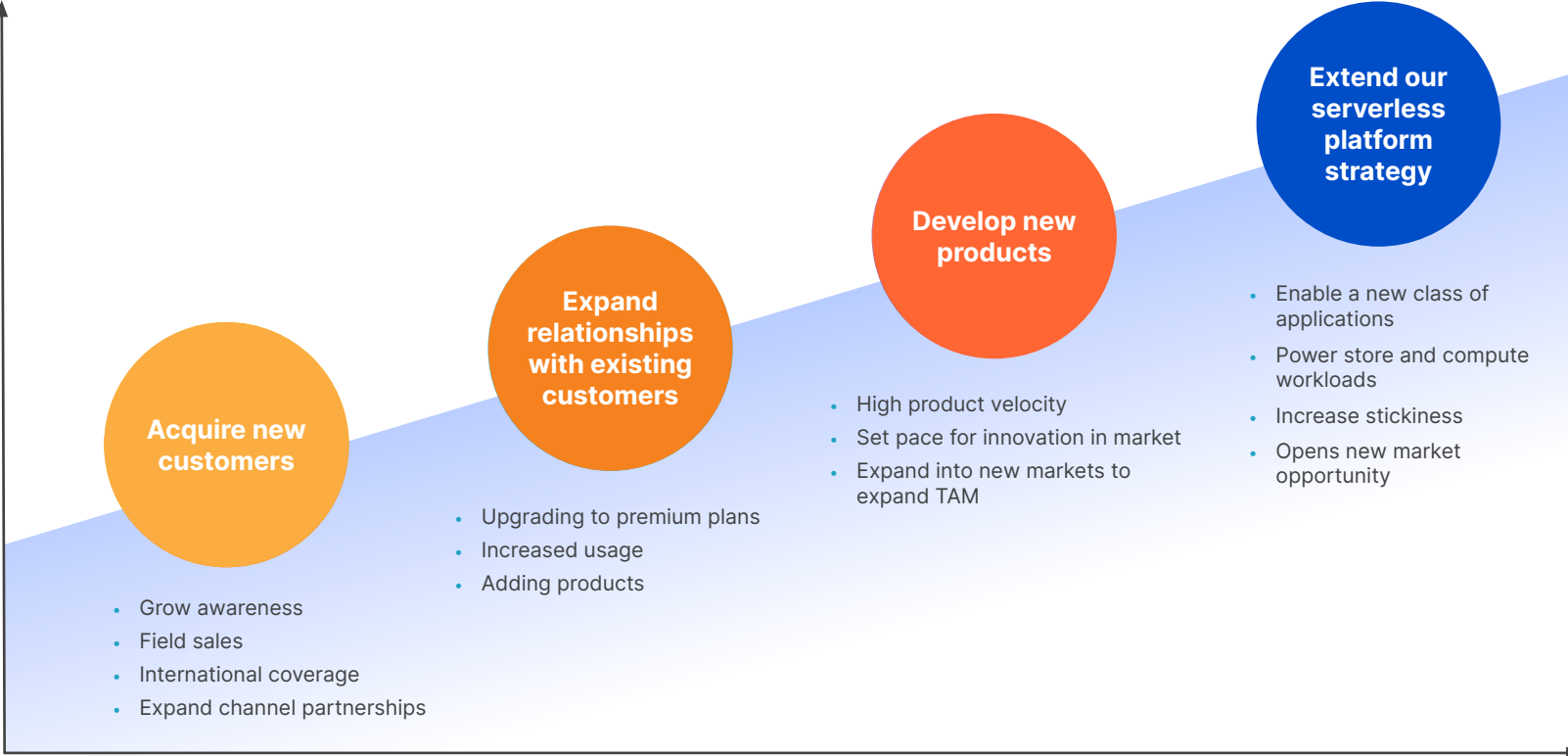
- Self service adoption for customers of all sizes
- Natural expansion
- Pulled into new geographies
- Pulled up market



CLOUDFLARE[®] Model



Our Strategy for Growth



Financial Overview

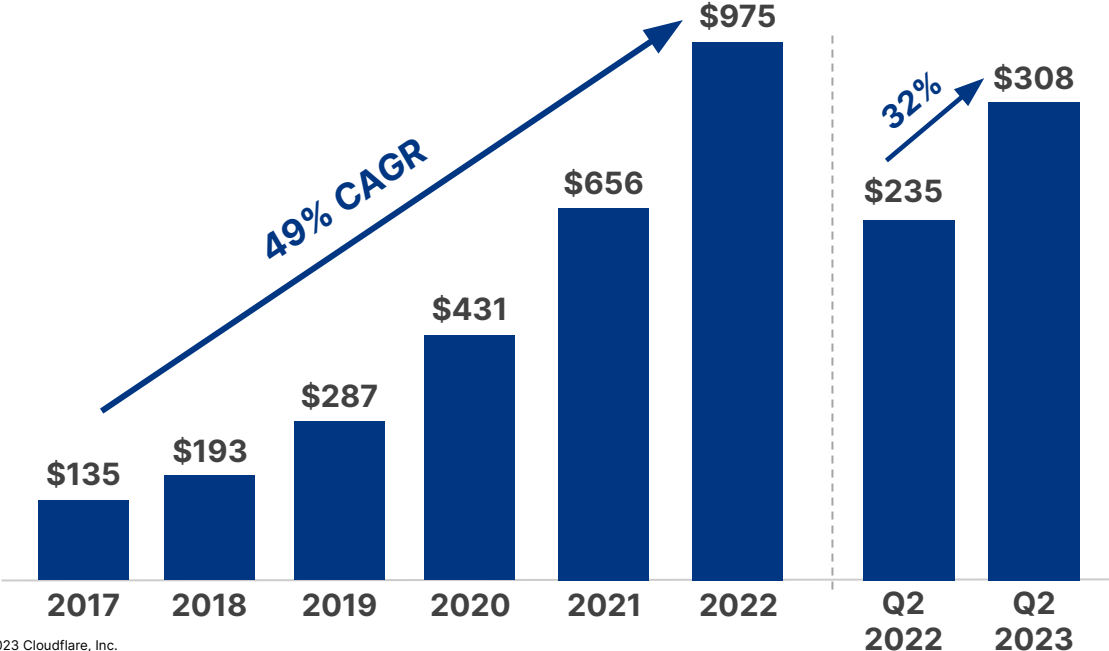
Key Financial Highlights



Note: Total Addressable Market represents 2023 expected spend from our analysis based on IDC data. Year-over-year revenue growth and gross margin are as of the three months ended June 30, 2023. Large Customers is as of June 30, 2023. See the Appendix for how we define "Large Customers."

Track Record of Delivering Revenue Growth

Total Revenue (\$M)



Investment in enterprise sales



Large customer momentum



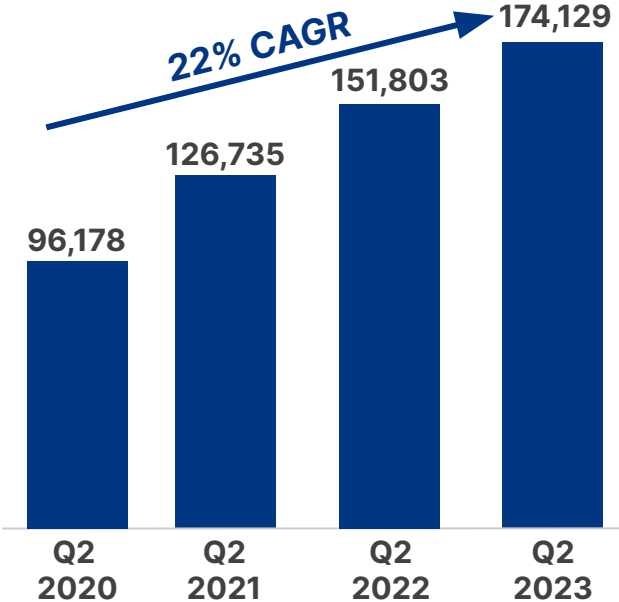
Land and expand strategy drives growth across cohorts



Strong penetration across the entire product portfolio

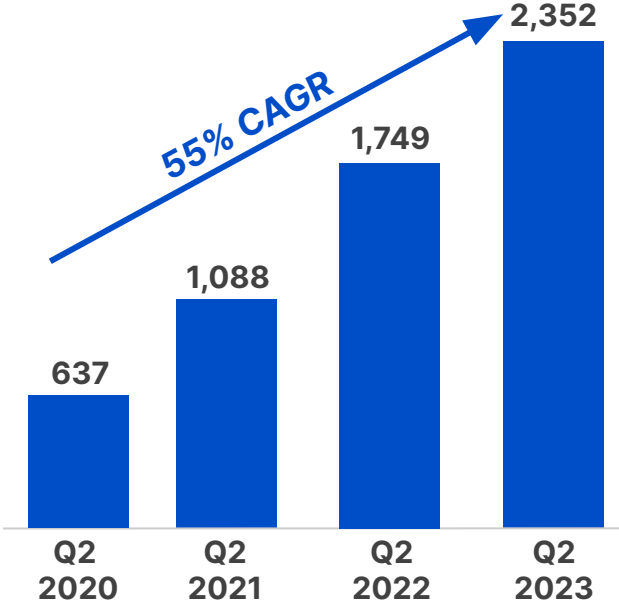
Rapid Customer Growth

Paying Customers



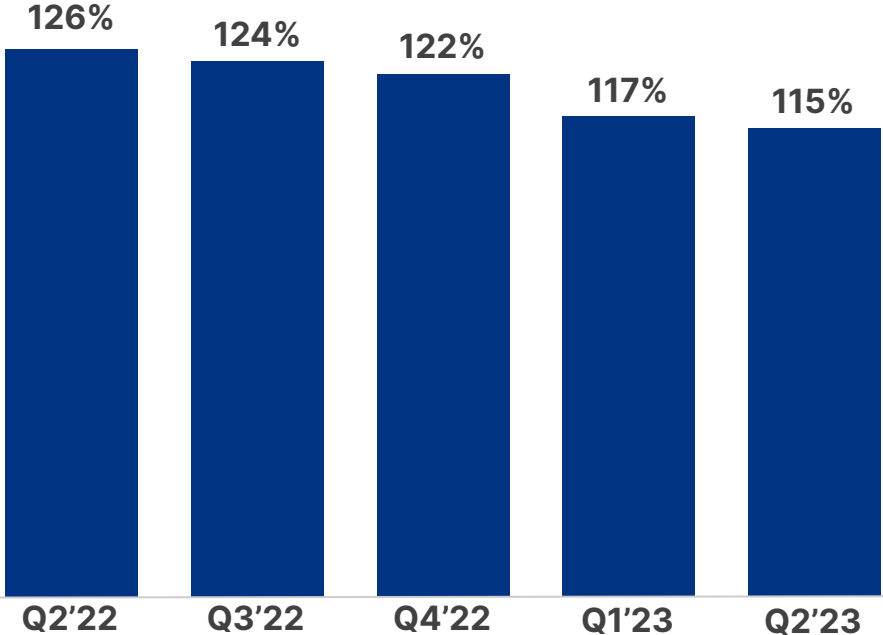
Large Customers

>\$100,000 Annualized Revenue



Note: See the Appendix for how we define "Paying Customers" and "Large Customers."

Strong Dollar-Based Net Retention



Note: See the Appendix for how we define “Dollar-Based Net Retention.”



DNR includes all paying customers



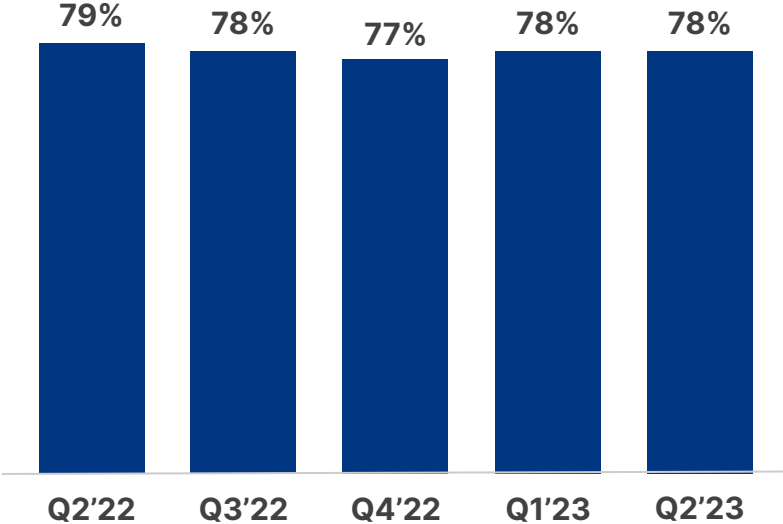
Large customers are a tailwind to DNR



Continuous innovation offers expansion opportunities

Attractive & Consistent Gross Margin

Non-GAAP Gross Margin



Serverless architecture deployed on commodity hardware

Single software stack across the network

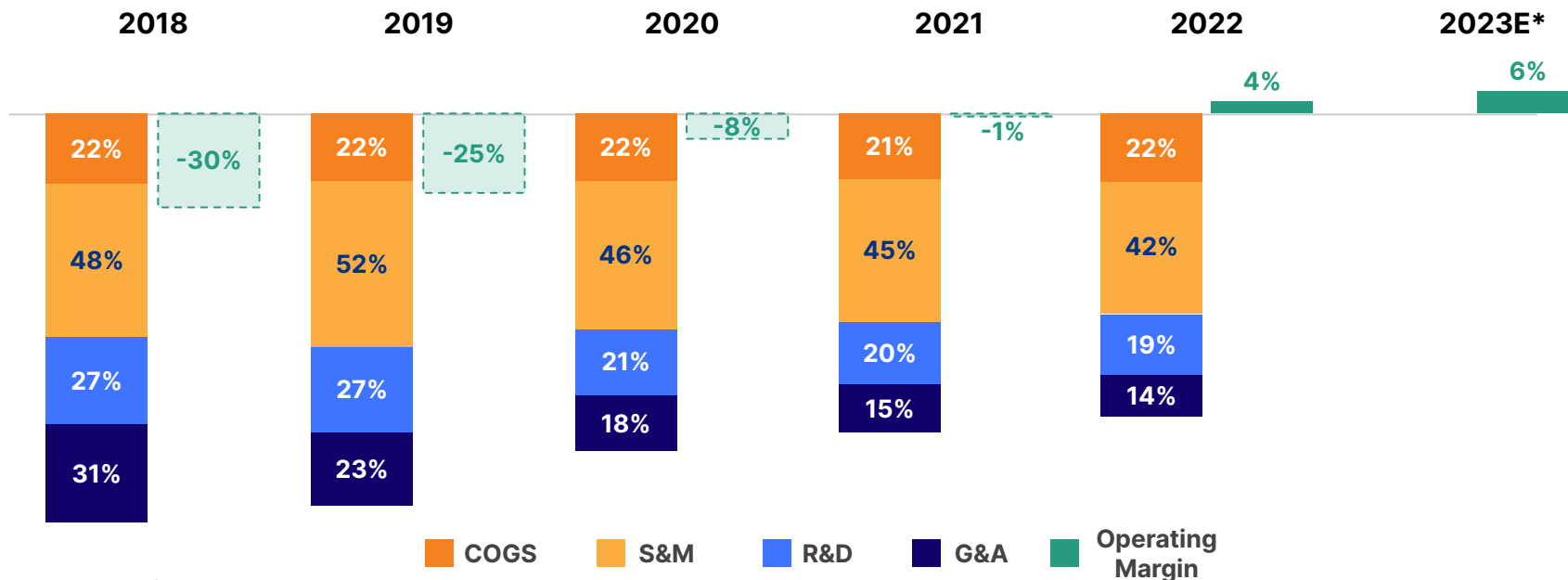
Symbiotic relationship with ISPs

Leverage idle capacity across network

Note: See Appendix for GAAP to Non-GAAP reconciliation.
© 2023 Cloudflare, Inc.

Elasticity of & Leverage in Our Operating Model

Non-GAAP Operating Expenses & Operating Income (% of Revenue)



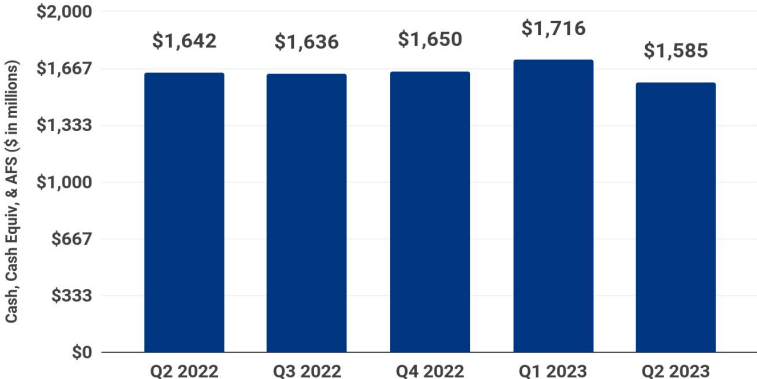
Note: See the Appendix for GAAP to Non-GAAP reconciliation.

*2023E is based on full-year mid-point guidance provided by us on August 3, 2023. Please refer to slide 28 for more details.

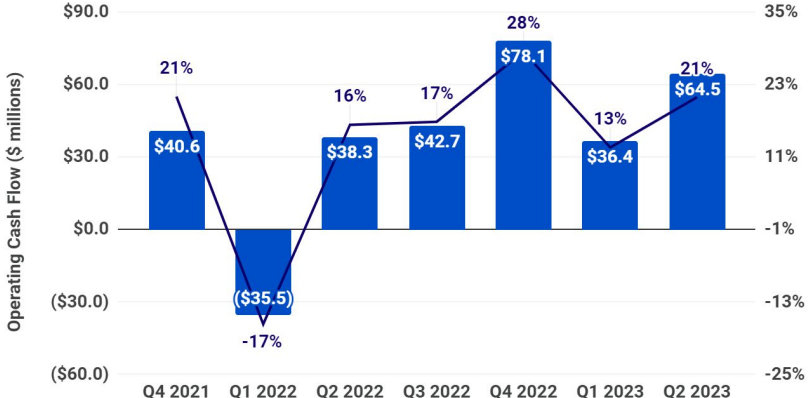
Strong Cash Position

- Issued 2025 Notes:** Raised \$495 million in our Convertible Notes Offering due 2025 that priced on May 13th, 2020, net of issuance costs and a capped call with respect to the 2025 convertible notes.
- Issued 2026 Notes:** Raised \$790 million in our Convertible Note Offering due 2026 that priced on August 10th, 2021, net of the repurchase of 2025 notes, issuance costs, and a capped call with respect to the 2026 convertible notes.
- Repurchased 2025 Notes:** Repurchased \$123.0 million principal amount for \$172.7 million in cash including accrued interest payable in May 2023. Paid approximately \$35.4 million in cash and delivered approximately 0.5 million shares of our Class A common stock in July 2023 to settle the conversion of approximately \$35.4 million aggregate principal amount of the 2025 Notes.

Cash Balance



Operating Cash Flow & Margin



Guidance

Q3 2023

Revenue **\$330.0 - 331.0**
Y/Y Growth 30%

Operating Income **\$20.0 - \$21.0**
Operating Margin 6%

EPS **\$0.10**

FY 2023

Revenue **\$1,283.0 - 1,287.0**
Y/Y Growth 32%

Operating Income **\$81.0 - \$85.0**
Operating Margin 6% - 7%

EPS **\$0.37**

FY 2023
Network Capex
as % of Revenue

10%-12%

Note: These forward looking statements were provided by us on August 3, 2023. This forward looking guidance speaks only as of such date and the inclusion of such guidance in this presentation should not be interpreted as a confirmation or affirmation of such guidance as of any other date. Except as required by law, we assume no obligation and do not intend to update these forward-looking statements or to conform these statements to actual results or to changes in our expectations.

Long-Term Operating Model

Unit economics support 20%+ long-term operating margins.

	2020	2021	2022	Q2 2023		Long-Term Model
Gross Margin	78 %	79 %	78 %	78 %	Leverage efficiency and elasticity of our network and ingress/egress dynamics	75% - 77%
Sales & Marketing (% of revenue)	46 %	45 %	42 %	41 %	Scale go-to-market operations with a focus on improving productivity	27% - 29%
Research & Development (% of revenue)	21 %	20 %	19 %	17 %	Continue to prioritize product innovation	18% - 20%
General & Administrative (% of revenue)	18 %	15 %	14 %	13 %	Benefit from economies of scale and automation	8% - 10%
Operating Margin	(8)%	(1)%	4%	7%		20%+
Free Cash Flow Margin	(21)%	(7)%	(4)%	6%		~25%+

Note: Metrics shown are Non-GAAP. See Appendix for GAAP financial measures and GAAP to Non-GAAP reconciliation.

Our Business Model



Disrupting a large and growing total addressable market



Widely distributed global cloud platform



Expansive product portfolio; open to developer innovation



Highly efficient business model and low fundamental cost structure



High growth subscription revenue model with attractive gross margin

Appendix

GAAP to Non-GAAP Reconciliation (Annual)

	2019	2020	2021	2022
GAAP Cost of Revenue	\$63,423	\$101,055	\$147,134	\$232,610
Less: Stock-based Compensation Expense & Related Payroll Taxes	-\$716	-\$1,466	-\$3,703	-\$6,770
Less: Amortization of Acquired Intangible Assets	-\$125	-\$3,081	-\$2,946	-\$13,444
Non-GAAP Cost of Revenue	\$62,582	\$96,508	\$140,485	\$212,396
GAAP Gross Profit	\$223,599	\$330,004	\$509,292	\$742,631
Add: Stock-based Compensation & Related Payroll Taxes	\$716	\$1,466	\$3,703	\$6,770
Add: Amortization of Acquired Intangible Assets	\$125	\$3,081	\$2,946	\$13,444
Non-GAAP Gross Profit	\$224,440	\$334,551	\$515,941	\$762,845
GAAP Gross Margin	78%	77%	78%	76%
Non-GAAP Gross Margin	78%	78%	79%	78%
GAAP Sales and Marketing	\$159,298	\$217,875	\$328,065	\$465,762
Less: Stock-based Compensation & Related Payroll Taxes	-\$8,709	-\$17,678	-\$32,869	-\$53,692
Less: Amortization of acquired intangible assets	-	-	-	-\$1,725
Less: Acquisition-related and other expenses	-	-	-	-\$265
Non-GAAP Sales and Marketing	\$150,589	\$200,197	\$295,196	\$410,080
GAAP S&M Expense as a % of Revenue	56%	51%	50%	48%
Non-GAAP S&M Expense as a % of Revenue	52%	46%	45%	42%
GAAP Research and Development	\$90,669	\$127,144	\$189,408	\$298,303
Less: Stock-based Compensation & Related Payroll Taxes	-\$13,037	-\$30,497	-\$61,056	-\$112,277
Less: Acquisition-related and other expenses	-	-\$5,725	-	-\$3,682
Non-GAAP Research and Development	\$77,632	\$90,922	\$128,352	\$182,344
GAAP R&D Expense as a % of Revenue	32%	29%	29%	31%
Non-GAAP R&D Expense as a % of Revenue	27%	21%	20%	19%
GAAP General and Administrative	\$81,578	\$91,753	\$119,503	\$179,769
Less: Stock-based Compensation & Related Payroll Taxes	-\$14,165	-\$13,875	-\$19,706	-\$45,027
Less: Acquisition-related and other expenses	-	-\$554	-\$380	\$0
Non-GAAP General and Administrative Expense	\$67,413	\$77,324	\$99,417	\$134,742
GAAP G&A Expense as a % of Revenue	28%	21%	18%	18%
Non-GAAP G&A Expense as a % of Revenue	23%	18%	15%	14%
GAAP Loss from Operations	-\$107,946	-\$106,768	-\$127,684	-\$201,203
Add: Stock-based Compensation & Related Payroll Taxes	\$36,627	\$63,516	\$117,334	\$217,766
Add: Amortization of Acquired Intangible Assets	\$125	\$3,081	\$2,946	\$15,169
Add: Acquisition-related and other expenses	-	\$6,279	\$380	\$3,947
Non-GAAP Loss from Operations	-\$71,194	-\$33,892	-\$7,024	\$35,679
GAAP Operating Margin	-38%	-25%	-19%	-21%
Non-GAAP Operating Margin	-25%	-8%	-1%	4%

GAAP to Non-GAAP Reconciliation (Quarterly)

	Q2 2022	Q3 2022	Q4 2022	Q1 2023	Q2 2023
GAAP Cost of Revenue	\$55,804	\$61,967	\$67,788	\$70,432	\$75,221
Less: Stock-based Compensation Expense & Related Payroll Taxes	-\$2,001	-\$2,157	-\$1,289	-\$1,803	-\$2,126
Less: Amortization of Acquired Intangible Assets	-\$4,312	-\$4,314	-\$4,311	-\$4,311	-\$4,314
Non-GAAP Cost of Revenue	\$49,491	\$55,496	\$62,188	\$64,318	\$68,781
GAAP Gross Profit	\$178,713	\$191,890	\$206,912	\$219,743	\$233,273
Add: Stock-based Compensation & Related Payroll Taxes	\$2,001	\$2,157	\$1,289	\$1,803	\$2,126
Add: Amortization of Acquired Intangible Assets	\$4,312	\$4,314	\$4,311	\$4,311	\$4,314
Non-GAAP Gross Profit	\$185,026	\$198,361	\$212,512	\$225,857	\$239,713
GAAP Gross Margin	76%	76%	75%	76%	76%
Non-GAAP Gross Margin	79%	78%	77%	78%	78%
GAAP Sales and Marketing	\$117,622	\$116,033	\$132,050	\$137,001	\$146,688
Less: Stock-based Compensation & Related Payroll Taxes	-\$12,907	-\$11,919	-\$18,487	-\$15,868	-\$20,734
Less: Amortization of acquired intangible assets	-\$575	-\$575	-\$575	-\$576	-\$574
Less: Acquisition-related and other expenses	-\$265	-	-	-	-
Non-GAAP Sales and Marketing	\$103,875	\$103,539	\$112,988	\$120,557	\$125,380
GAAP S&M Expense as a % of Revenue	50%	46%	48%	47%	48%
Non-GAAP S&M Expense as a % of Revenue	44%	41%	41%	42%	41%
GAAP Research and Development	\$75,114	\$76,432	\$79,703	\$81,539	\$89,610
Less: Stock-based Compensation & Related Payroll Taxes	-\$27,873	-\$30,049	-\$30,276	-\$30,216	-\$36,573
Less: Acquisition-related and other expenses	-\$1,043	-	-	-	-
Non-GAAP Research and Development	\$46,198	\$46,383	\$49,427	\$51,323	\$53,037
GAAP R&D Expense as a % of Revenue	32%	30%	29%	28%	29%
Non-GAAP R&D Expense as a % of Revenue	20%	18%	18%	18%	17%
GAAP General and Administrative	\$50,518	\$45,372	\$45,850	\$48,475	\$53,147
Less: Stock-based Compensation & Related Payroll Taxes	-\$14,674	-\$11,763	-\$12,572	-\$13,863	-\$12,156
Non-GAAP General and Administrative Expense	\$35,844	\$33,609	\$33,278	\$34,612	\$40,991
GAAP G&A Expense as a % of Revenue	22%	18%	17%	17%	17%
Non-GAAP G&A Expense as a % of Revenue	15%	13%	12%	12%	13%
GAAP Loss from Operations	-\$64,541	-\$45,947	-\$50,691	-\$47,272	-\$56,172
Add: Stock-based Compensation & Related Payroll Taxes	\$57,455	\$55,888	\$62,624	\$61,750	\$71,589
Add: Amortization of Acquired Intangible Assets	\$4,887	\$4,889	\$4,886	\$4,887	\$4,888
Add: Acquisition-related and other expenses	\$1,308	-	-	-	-
Non-GAAP Loss from Operations	-\$891	\$14,830	\$16,819	\$19,365	\$20,305
GAAP Operating Margin	-28%	-18%	-18%	-16%	-18%
Non-GAAP Operating Margin	0%	6%	6%	7%	7%

Key Business Metrics

Paying Customers

	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	Q2 2023
	132,390	140,096	148,184	151,803	156,000	162,086	168,159	174,129
y-y growth	31%	26%	24%	20%	18%	16%	13%	15%

Paying Customers (> \$100,000 Annualized Revenue)

	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	Q2 2023
	1,260	1,416	1,537	1,749	1,908	2,042	2,156	2,352
y-y growth	71%	71%	63%	61%	51%	44%	40%	34%
% of revenue	55%	57%	58%	60%	61%	63%	62%	64%

Dollar-Based Net Retention

	Q3 2021	Q4 2021	Q1 2022	Q2 2022	Q3 2022	Q4 2022	Q1 2023	Q2 2023
	124%	125%	127%	126%	124%	122%	117%	115%

Note: See next slide for definitions of Paying Customers, Paying Customers (> \$100,000 Annualized Revenue), and Dollar-Based Net Retention.

Definitions

Paying Customers. We believe our ability to grow the number of paying customers on our network provides a key indicator of growth of our business and our future business opportunities. We define a paying customer at the end of the quarter as a person or entity who has generated revenue and has an active contract with us or one of our partners during such quarter, excluding (i) customers that were not acquired through ordinary sales channels, (ii) customers using only our registrar product, and (iii) customers using our consumer applications, such as 1.1.1 and Warp, which agreements and customers together represent an insignificant amount of our revenue. An entity is defined as a company, a government institution, a non-profit organization, or a distinct business unit of a large company. An active contract is defined as a customer relationship for which we have provided services during the quarter.

Paying Customers (> \$100,000 Annualized Revenue). While we continue to grow customers across all sizes, over time, our large customers have contributed an increasing share of our revenue. We view the number of customers with Annualized Revenue greater than \$100,000 as indicative of our penetration within large enterprise accounts. To measure Annualized Revenue at the end of a quarter, we take the sum of revenue for each customer in the quarter and multiply that amount by four. For example, if we signed a new customer that generated \$1,800 of revenue in a quarter, that customer would account for \$7,200 of Annualized Revenue for that year. Our Annualized Revenue calculation excludes (i) agreements that were not entered into through ordinary sales channels, (ii) revenue generated from customers using only our registrar product, and (iii) customers using our consumer applications, such as 1.1.1 and Warp, which agreements and customers together represent an insignificant amount of our revenue. Our Annualized Revenue metric also includes any usage charges by a customer during a period, which represents a small portion of our total revenue and may not be recurring. As a result, Annualized Revenue may be higher than actual revenue over the course of the year.

Dollar-Based Net Retention. Our ability to maintain long-term revenue growth and achieve profitability is dependent on our ability to retain and grow revenue generated from our existing paying customers. We believe that we will achieve these objectives by continuing to focus on customer loyalty and adding additional products and functionality to our network. Our dollar-based net retention rate is a key way we measure our performance in these areas. Dollar-based net retention measures our ability to retain and expand recurring revenue from existing customers. To calculate dollar-based net retention for a quarter, we compare the Annualized Revenue from paying customers four quarters prior to the Annualized Revenue from the same set of customers in the most recent quarter. Our dollar-based net retention includes expansion and is net of contraction and attrition, but excludes Annualized Revenue from new customers in the current period. Our dollar-based net retention excludes the benefit of free customers that upgrade to a paid subscription between the prior and current periods, even though this is an important source of incremental growth. We believe this provides a more meaningful representation of our ability to add incremental business from existing paying customers as they renew and expand their contracts.