

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**
Washington, D.C. 20549

FORM 10-Q

(Mark One)

☒ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended December 31, 2022
or

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from to

Commission File Number: 001-38603

SONOS, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction
of incorporation or organization)

03-0479476
(I.R.S. Employer Identification No.)

614 Chapala Street
(Address of Principal Executive Offices)

Santa Barbara

CA

93101
(Zip Code)

(805) 965-3001

Registrant's telephone number, including area code

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, \$0.001 par value	SONO	The Nasdaq Stock Market LLC

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ☒ No ☐

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company", and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	☒	Accelerated filer	☐
Non-accelerated filer	☐	Smaller reporting company	☐
		Emerging growth company	☐

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ☐ No ☒

As of January 31, 2023, the registrant had 127,347,882 shares of common stock outstanding.

TABLE OF CONTENTS

	<u>Page</u>
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1.</u>	<u>Financial Statements (unaudited)</u>
	<u>Condensed consolidated balance sheets</u> 3
	<u>Condensed consolidated statements of operations and comprehensive income</u> 4
	<u>Condensed consolidated statements of stockholders' equity</u> 5
	<u>Condensed consolidated statements of cash flows</u> 6
	<u>Notes to condensed consolidated financial statements</u> 7
<u>Item 2.</u>	<u>Management's discussion and analysis of financial condition and results of operations</u> 20
<u>Item 3.</u>	<u>Quantitative and qualitative disclosures about market risk</u> 31
<u>Item 4.</u>	<u>Controls and procedures</u> 32
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1.</u>	<u>Legal proceedings</u> 33
<u>Item 1A.</u>	<u>Risk factors</u> 33
<u>Item 2.</u>	<u>Unregistered sales of equity securities and use of proceeds</u> 49
<u>Item 3.</u>	<u>Defaults upon senior securities</u> 49
<u>Item 4.</u>	<u>Mine safety disclosures</u> 49
<u>Item 5.</u>	<u>Other information</u> 49
<u>Item 6.</u>	<u>Exhibit index</u> 50
<u>SIGNATURES</u>	51

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

SONOS, INC. CONDENSED CONSOLIDATED BALANCE SHEETS *(unaudited, in thousands, except par values)*

	As of	
	December 31, 2022	October 1, 2022
Assets		
Current assets:		
Cash and cash equivalents	\$ 431,533	\$ 274,855
Accounts receivable, net of allowances	109,703	101,206
Inventories	306,056	454,288
Prepays and other current assets	34,765	37,042
Total current assets	882,057	867,391
Property and equipment, net	85,068	86,168
Operating lease right-of-use assets	25,894	28,329
Goodwill	80,941	77,300
Intangible assets, net		
In-process research and development	70,640	64,680
Other intangible assets	24,705	26,384
Deferred tax assets	1,416	1,508
Other noncurrent assets	36,154	36,628
Total assets	<u>\$ 1,206,875</u>	<u>\$ 1,188,388</u>
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	\$ 236,037	\$ 335,758
Accrued expenses	138,344	109,290
Accrued compensation	26,430	23,624
Deferred revenue, current	19,560	27,318
Other current liabilities	57,268	39,649
Total current liabilities	477,639	535,639
Operating lease liabilities, noncurrent	22,318	25,596
Deferred revenue, noncurrent	62,421	56,152
Deferred tax liabilities	10,415	9,642
Other noncurrent liabilities	728	846
Total liabilities	<u>573,521</u>	<u>627,875</u>
Commitments and contingencies (Note 7)		
Stockholders' equity:		
Common stock, \$0.001 par value	130	130
Treasury stock	(35,047)	(50,896)
Additional paid-in capital	606,420	617,390
Retained earnings (accumulated deficit)	72,674	(2,514)
Accumulated other comprehensive loss	(10,823)	(3,597)
Total stockholders' equity	633,354	560,513
Total liabilities and stockholders' equity	<u>\$ 1,206,875</u>	<u>\$ 1,188,388</u>

The accompanying notes are an integral part of these condensed consolidated financial statements.

SONOS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME
(unaudited, in thousands, except share and per share amounts)

	Three Months Ended	
	December 31, 2022	January 1, 2022
Revenue	\$ 672,579	\$ 664,481
Cost of revenue	387,522	347,096
Gross profit	285,057	317,385
Operating expenses		
Research and development	76,940	61,330
Sales and marketing	78,696	83,736
General and administrative	43,117	39,725
Total operating expenses	198,753	184,791
Operating income	86,304	132,594
Other income (expense), net		
Interest income	1,967	33
Interest expense	(158)	(98)
Other income (expense), net	23,576	(1,402)
Total other income (expense), net	25,385	(1,467)
Income before provision for income taxes	111,689	131,127
Provision for income taxes	36,501	7,646
Net income	\$ 75,188	\$ 123,481
Net income attributable to common stockholders:		
Basic and diluted	\$ 75,188	\$ 123,481
Net income per share attributable to common stockholders:		
Basic	\$ 0.59	\$ 0.97
Diluted	\$ 0.57	\$ 0.87
Weighted-average shares used in computing net income per share attributable to common stockholders:		
Basic	127,212,245	127,662,826
Diluted	131,502,986	142,322,448
Total comprehensive income		
Net income	75,188	123,481
Change in foreign currency translation adjustment	(7,226)	(360)
Comprehensive income	\$ 67,962	\$ 123,121

The accompanying notes are an integral part of these condensed consolidated financial statements.

SONOS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(unaudited, in thousands, except share amounts)

	Common Stock			Treasury Stock		Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
	Shares	Amount	Additional Paid-In Capital	Shares	Amount			
Balance at October 1, 2022	129,823,663	\$ 130	\$ 617,390	(3,154,940)	\$ (50,896)	\$ (2,514)	\$ (3,597)	\$ 560,513
Issuance of common stock pursuant to equity incentive plans	1,973,506	2	8,101	—	—	—	—	8,103
Retirement of treasury stock	(2,293,416)	(2)	(39,266)	2,293,416	39,268	—	—	—
Repurchase of common stock	—	—	—	(849,806)	(15,043)	—	—	(15,043)
Repurchase of common stock related to shares withheld for tax in connection with vesting of stock awards	—	—	—	(470,585)	(8,376)	—	—	(8,376)
Stock-based compensation expense	—	—	20,195	—	—	—	—	20,195
Net income	—	—	—	—	—	75,188	—	75,188
Change in foreign currency translation adjustment	—	—	—	—	—	—	(7,226)	(7,226)
Balance at December 31, 2022	129,503,753	\$ 130	\$ 606,420	(2,181,915)	\$ (35,047)	\$ 72,674	\$ (10,823)	\$ 633,354

	Common Stock			Treasury Stock		Retained Earnings (Accumulated Deficit)	Accumulated Other Comprehensive Loss	Total Stockholders' Equity
	Shares	Amount	Additional Paid-In Capital	Shares	Amount			
Balance at October 2, 2021	128,857,085	\$ 129	\$ 690,462	(1,871,812)	\$ (50,276)	\$ (69,897)	\$ (1,376)	\$ 569,042
Issuance of common stock pursuant to equity incentive plans	2,030,373	2	13,230	—	—	—	—	13,232
Retirement of treasury stock	(1,010,286)	(1)	(38,647)	1,010,286	38,648	—	—	—
Repurchase of common stock	—	—	—	(1,032,249)	(31,365)	—	—	(31,365)
Repurchase of common stock related to shares withheld for tax in connection with vesting of stock awards	—	—	—	(344,198)	(11,882)	—	—	(11,882)
Stock-based compensation expense	—	—	17,459	—	—	—	—	17,459
Net income	—	—	—	—	—	123,481	—	123,481
Change in foreign currency translation adjustment	—	—	—	—	—	—	(360)	(360)
Balance at January 1, 2022	129,877,172	\$ 130	\$ 682,504	(2,237,973)	\$ (54,875)	\$ 53,584	\$ (1,736)	\$ 679,607

The accompanying notes are an integral part of these condensed consolidated financial statements.

SONOS, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited, in thousands)

	Three Months Ended	
	December 31, 2022	January 1, 2022
Cash flows from operating activities		
Net income	\$ 75,188	\$ 123,481
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	11,132	9,217
Stock-based compensation expense	20,195	17,459
Other	6,797	1,139
Deferred income taxes	167	14
Foreign currency transaction (gains) losses	(17,700)	494
Changes in operating assets and liabilities:		
Accounts receivable, net	(7,286)	(79,000)
Inventories	143,144	(21,800)
Other assets	2,463	4,086
Accounts payable and accrued expenses	(65,917)	185,127
Accrued compensation	2,249	(49,094)
Deferred revenue	(3,950)	(13,510)
Other liabilities	15,804	2,321
Net cash provided by operating activities	<u>182,286</u>	<u>179,934</u>
Cash flows from investing activities		
Purchases of property and equipment, and intangible assets	(14,689)	(6,355)
Cash paid for acquisitions, net of acquired cash	—	(27,101)
Net cash used in investing activities	<u>(14,689)</u>	<u>(33,456)</u>
Cash flows from financing activities		
Payments for debt issuance costs	—	(929)
Payments for repurchase of common stock	(15,043)	(31,365)
Proceeds from exercise of common stock options	8,103	13,232
Payments for repurchase of common stock related to shares withheld for tax in connection with vesting of stock awards	(8,376)	(11,882)
Net cash used in financing activities	<u>(15,316)</u>	<u>(30,944)</u>
Effect of exchange rate changes on cash and cash equivalents	4,397	(1,218)
Net increase in cash and cash equivalents	<u>156,678</u>	<u>114,316</u>
Cash and cash equivalents		
Beginning of period	274,855	640,101
End of period	<u>\$ 431,533</u>	<u>\$ 754,417</u>
Supplemental disclosure		
Cash paid for interest	\$ 111	\$ 23
Cash paid for taxes, net of refunds	\$ 1,903	\$ 413
Cash paid for amounts included in the measurement of lease liabilities	\$ 2,190	\$ 3,410
Supplemental disclosure of non-cash investing and financing activities		
Purchases of property and equipment in accounts payable and accrued expenses	\$ 2,030	\$ 5,499
Right-of-use assets obtained in exchange for new operating lease liabilities	\$ —	\$ 2,246

The accompanying notes are an integral part of these condensed consolidated financial statements.

SONOS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. Business Overview and Basis of Presentation

Description of business

Sonos, Inc. and its wholly owned subsidiaries (collectively, “Sonos,” the “Company,” “we,” “us” or “our”) designs, develops, manufactures, and sells audio products and services. The Sonos sound system provides customers with an immersive listening experience created by the design of its speakers and components, a proprietary software platform, and the ability to stream content from a variety of sources over the customer’s wireless network or over Bluetooth.

The Company’s products are sold through third-party physical retailers, including custom installers of home audio systems, select e-commerce retailers, and its website, sonos.com. The Company’s products are distributed in over 60 countries through its wholly owned subsidiaries: Sonos Europe B.V. in the Netherlands, Beijing Sonos Technology Co. Ltd. in China, Sonos Japan GK in Japan, and Sonos Australia Pty Ltd. in Australia.

Basis of presentation and preparation

The accompanying condensed consolidated financial statements are unaudited. The condensed consolidated balance sheet as of October 1, 2022, has been derived from the audited consolidated financial statements of the Company.

The accompanying condensed consolidated financial statements have been prepared in accordance with generally accepted accounting principles in the United States of America (“U.S. GAAP”) for interim financial information and the applicable rules and regulations of the Securities and Exchange Commission (“SEC”). Accordingly, they do not include all the information and footnotes required by U.S. GAAP for annual financial statements. They should be read in conjunction with the consolidated financial statements and notes thereto contained in the Company’s Annual Report on Form 10-K for the fiscal year ended October 1, 2022, (the “Annual Report”), filed with the SEC on November 23, 2022.

In management’s opinion, the accompanying unaudited condensed consolidated financial statements include all adjustments, consisting of only normal recurring adjustments, necessary for the fair statement of the Company’s financial position, its results of operations, and its cash flows for the interim periods presented. The results of operations for the three months ended December 31, 2022, are not necessarily indicative of the results to be expected for the full fiscal year or any other period.

The Company operates on a 52- week or 53- week fiscal year ending on the Saturday nearest September 30 each year. The Company’s fiscal year is divided into four quarters of 13 weeks, each beginning on a Sunday and containing two 4-week periods followed by a 5-week period. An additional week is included in the fourth fiscal quarter approximately every five years to realign fiscal quarters with calendar quarters. This last occurred in the fourth quarter of the Company’s fiscal year ended October 3, 2020, and will reoccur in the fiscal year ending October 3, 2026. The three months ended December 31, 2022, and January 1, 2022, spanned 13 weeks each. As used in this Quarterly Report on Form 10-Q, “fiscal 2023” refers to the fiscal year ending September 30, 2023, “fiscal 2022” refers to the fiscal year ended October 1, 2022, “fiscal 2021” refers to the fiscal year ended October 2, 2021, and “fiscal 2020” refers to the fiscal year ended October 3, 2020.

Use of estimates and judgments

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and judgments that affect the amounts reported and disclosed in the condensed consolidated financial statements and accompanying notes. Actual results could differ materially from those estimates. On an ongoing basis, the Company evaluates its estimates and judgments compared to historical experience and expected trends.

The Company has considered the impacts of the COVID-19 pandemic when developing its estimates and assumptions noted above. The impacts of, and uncertainty related to, the COVID-19 pandemic and its expected duration persist. Actual results and outcomes may differ from management's estimates and assumptions.

SONOS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(unaudited)

2. Summary of Significant Accounting Policies

There have been no changes in the Company's significant accounting policies, recently adopted accounting pronouncements or recent accounting pronouncements pending adoption from those disclosed in the Annual Report, except as noted below.

Recent accounting pronouncements pending adoption

In March 2020, the FASB issued ASU No. 2020-04, Reference Rate Reform (Topic 848): Facilitation of Effects of Reference Rate Reform on Financial Reporting, and then issued subsequent amendments to the initial guidance under ASU No. 2021-01 and ASU No. 2022-06 (collectively Topic 848). Topic 848 provides practical expedients and exceptions for applying U.S. GAAP to contracts, hedging relationships, derivatives, and other transactions affected by reference rate reform if certain criteria are met. The expedients and exceptions provided by the amendments in this update apply only to contracts, hedging relationships, derivatives, and other transactions that reference the London interbank offered rate ("LIBOR") or another reference rate expected to be discontinued as a result of reference rate reform. Topic 848 is currently effective and upon adoption may be applied prospectively to contract modifications and hedging relationships made on or before December 31, 2024. The Company is currently evaluating the pronouncement to determine the impact it may have on the Company's consolidated financial statements.

3. Fair Value Measurements

The carrying values of the Company's financial instruments, including accounts receivable and accounts payable, approximate their fair values due to the short period of time to maturity or repayment.

The following table summarizes fair value measurements by level for the assets measured at fair value on a recurring basis as of December 31, 2022, and October 1, 2022:

		December 31, 2022			
		Level 1	Level 2	Level 3	Total
(In thousands)					
Assets:					
Money market funds (cash equivalents)		\$ 302,799	\$ —	\$ —	\$ 302,799
		October 1, 2022			
		Level 1	Level 2	Level 3	Total
(In thousands)					
Assets:					
Money market funds (cash equivalents)		\$ 187,170	\$ —	\$ —	\$ 187,170

SONOS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(unaudited)

4. Revenue and Geographic Information

Disaggregation of revenue

Revenue is attributed to each region based on ship-to address, and also includes the applicable service revenue for software upgrades and cloud-based services attributable to each region. Revenue by region is as follows:

	Three Months Ended	
	December 31, 2022	January 1, 2022
(In thousands)		
Americas	\$ 396,565	\$ 373,813
Europe, Middle East and Africa ("EMEA")	240,439	245,482
Asia Pacific ("APAC")	35,575	45,186
Total revenue	<u>\$ 672,579</u>	<u>\$ 664,481</u>

Revenue is attributed to individual countries based on ship-to address and also includes the applicable service revenue for software upgrades and cloud-based services attributable to each country. Revenue by significant countries is as follows:

	Three Months Ended	
	December 31, 2022	January 1, 2022
(In thousands)		
United States	\$ 365,974	\$ 347,646
Other countries	306,605	316,835
Total revenue	<u>\$ 672,579</u>	<u>\$ 664,481</u>

Revenue by product category also includes the applicable service revenue for software upgrades and cloud-based services attributable to each product category. Revenue by major product category is as follows:

	Three Months Ended	
	December 31, 2022	January 1, 2022
(In thousands)		
Sonos speakers	\$ 539,196	\$ 501,886
Sonos system products	114,434	134,745
Partner products and other revenue	18,949	27,850
Total revenue	<u>\$ 672,579</u>	<u>\$ 664,481</u>

5. Balance Sheet Components

Accounts receivable, net of allowances

Accounts receivable, net of allowances, consist of the following:

	December 31, 2022	October 1, 2022
(In thousands)		
Accounts receivable	\$ 141,587	\$ 127,523
Allowance for credit losses	(3,129)	(2,744)
Allowance for sales incentives	(28,755)	(23,573)
Accounts receivable, net of allowances	<u>\$ 109,703</u>	<u>\$ 101,206</u>

SONOS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(unaudited)

Inventories

Inventories, net, consist of the following:

	December 31, 2022	October 1, 2022
(In thousands)		
Finished goods	\$ 260,734	\$ 406,657
Component parts	45,322	47,631
Inventories	<u>\$ 306,056</u>	<u>\$ 454,288</u>

The Company writes down inventory as a result of excess and obsolete inventories or when it believes that the net realizable value of inventories is less than the carrying value. As of December 31, 2022, and October 1, 2022, inventory write-downs were \$15.2 million and \$8.8 million, respectively.

Goodwill

The following table presents the changes in carrying amount of goodwill during the three months ended December 31, 2022:

(In thousands)	
Balance as of October 1, 2022	\$ 77,300
Effect of exchange rate changes on goodwill	3,641
Balance as of December 31, 2022	<u>\$ 80,941</u>

Intangible assets

The following table reflects the changes in the net carrying amount of the components of intangible assets associated with the Company's acquisition activity:

	December 31, 2022				
(In thousands, except weighted-average remaining life)	Gross Carrying Amount	Accumulated Amortization	Impact of FX	Net Carrying Value	Weighted- Average Remaining Life
Trade name	\$ 451	\$ (52)	\$ (7)	\$ 392	5.25
Technology-based	31,480	(7,167)	—	24,313	5.36
Total finite-lived intangible assets	31,931	(7,219)	(7)	24,705	5.36
In-process research and development not subject to amortization	71,759	—	(1,119)	70,640	
Total intangible assets	<u>\$ 103,690</u>	<u>\$ (7,219)</u>	<u>\$ (1,126)</u>	<u>\$ 95,345</u>	

SONOS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(unaudited)

The following table summarizes the estimated future amortization expense of the Company's intangible assets as of December 31, 2022:

Fiscal years ending (In thousands)	Future Amortization Expense
Remainder of fiscal 2023	\$ 4,478
2024	5,970
2025	3,369
2026	3,040
2027	3,025
2028 and there after	4,823
Total future amortization expense	<u>\$ 24,705</u>

Cloud Computing Arrangements

The Company incurs costs to implement cloud computing arrangements that are hosted by a third-party vendor. Implementation costs incurred during the application development stage are capitalized until the software is ready for its intended use. The costs are then amortized on a straight-line basis over the term of the associated hosting arrangement and are recognized as an operating expense within the condensed consolidated statements of operations and comprehensive income. Beginning in fiscal 2020, and continuing through April 2022, the Company conducted activities to replace its legacy enterprise resource management system in order to accommodate the Company's expanding operations. In May 2022, the Company went live with its implementation of a new enterprise resource planning ("ERP") system. Capitalized costs, net of accumulated amortization, were \$20.7 million and \$21.7 million as of December 31, 2022, and October 1, 2022, respectively, and are reported as a component of other noncurrent assets on the Company's condensed consolidated balance sheets. Amortization expenses for implementation costs for cloud-based computing arrangements for three months ended December 31, 2022 were \$1.0 million. Accumulated amortization was \$3.5 million and \$2.5 million as of December 31, 2022, and October 1, 2022, respectively.

Accrued expenses

Accrued expenses consisted of the following:

(In thousands)	December 31, 2022	October 1, 2022
Accrued taxes	\$ 52,729	\$ 7,081
Accrued inventory and supply chain costs	44,895	51,011
Accrued general and administrative expenses	21,124	21,634
Accrued advertising and marketing	12,893	21,292
Accrued product development	6,392	8,168
Other accrued payables	311	104
Total accrued expenses	<u>\$ 138,344</u>	<u>\$ 109,290</u>

SONOS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(unaudited)

Deferred revenue

Amounts invoiced in advance of revenue recognition are recorded as deferred revenue on the condensed consolidated balance sheets. Deferred revenue primarily relates to revenue allocated to unspecified software upgrades and cloud-based services. Recognition of revenue as of December 31, 2022, includes \$9.2 million of deferred revenue from the fourth quarter of fiscal 2022, related to newly launched products sold to resellers not recognized as revenue until the date of general availability was reached, which was the first quarter of fiscal 2023. Recognition of revenue as of January 1, 2022, includes \$18.8 million of deferred revenue from the fourth quarter of fiscal 2021, related to newly launched products sold to resellers not recognized as revenue until the date of general availability was reached, which was the first quarter of fiscal 2022.

The following table presents the changes in the Company's deferred revenue for the three months ended December 31, 2022, and January 1, 2022:

	December 31, 2022	January 1, 2022
(In thousands)		
Deferred revenue, beginning of period	\$ 83,470	\$ 89,498
Recognition of revenue included in beginning of period deferred revenue	(11,520)	(23,721)
Revenue deferred, net of revenue recognized on contracts in the respective period	10,031	9,801
Deferred revenue, end of period	<u>\$ 81,981</u>	<u>\$ 75,578</u>

The Company expects the following recognition of deferred revenue as of December 31, 2022:

	For the fiscal years ending					
	2023	2024	2025	2026	2027 and Beyond	Total
(In thousands)						
Deferred revenue expected to be recognized	\$ 14,954	\$ 17,507	\$ 15,214	\$ 12,830	\$ 21,476	\$ 81,981

Other current liabilities

Other current liabilities consist of the following:

	December 31, 2022	October 1, 2022
(In thousands)		
Reserve for returns	\$ 21,197	\$ 18,263
Short-term operating lease liabilities	10,827	10,532
Warranty liability	9,917	5,771
Other	15,327	5,083
Total other current liabilities	<u>\$ 57,268</u>	<u>\$ 39,649</u>

SONOS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(unaudited)

The following table presents the changes in the Company's warranty liability for the three months ended December 31, 2022, and January 1, 2022:

(In thousands)	December 31, 2022	January 1, 2022
Warranty liability, beginning of period	\$ 5,771	\$ 5,604
Provision for warranties issued during the period	6,177	5,359
Settlements of warranty claims during the period	(2,031)	(1,297)
Warranty liability, end of period	<u>\$ 9,917</u>	<u>\$ 9,666</u>

6. Debt

On October 13, 2021, the Company entered into a Revolving Credit Agreement with JPMorgan Chase Bank, N.A., as the administrative agent, and the lenders party thereto (the "Revolving Credit Agreement").

The Revolving Credit Agreement provides for (i) a five-year senior secured revolving credit facility in the amount of up to \$100.0 million and (ii) an uncommitted incremental facility subject to certain conditions. Proceeds are to be used for working capital and general corporate purposes. The facility may be drawn as an Alternative Base Rate Loan (at 1.00% plus an applicable margin) or Eurocurrency Loans (at LIBOR plus an applicable margin). The Company must also pay (i) an unused commitment fee ranging from 0.200% to 0.275% per annum of the average daily unused portion of the aggregate revolving credit commitment under the agreement and (ii) a per annum fee equal to the applicable margin over LIBOR multiplied by the aggregate face amount of outstanding letters of credit. As of December 31, 2022, the Company did not have any outstanding borrowings and had \$3.0 million in undrawn letters of credit that reduce the availability under the Revolving Credit Agreement.

The Company's obligations under the Revolving Credit Agreement are secured by substantially all of the Company's assets. The Revolving Credit Agreement contains customary representations and warranties, customary affirmative and negative covenants, a financial covenant that is tested quarterly and requires the Company to maintain a certain consolidated leverage ratio, and customary events of default. As of December 31, 2022, the Company was in compliance with all financial covenants under the Revolving Credit Agreement.

7. Commitments and Contingencies

Commitments to suppliers

At December 31, 2022, the Company's commitments to suppliers were estimated to be approximately \$260 million, the majority of which is expected to be paid in the next two years, with approximately \$126 million to \$150 million expected to be paid in the next twelve months. These commitments are related to electrical components that are specific to Sonos products, and for which the Company typically participates in negotiations directly with the suppliers, and included 1) contractual obligations to third-party manufacturers and suppliers, 2) the inventory owned by contract manufacturers procured to manufacture Sonos products, and 3) purchase commitments made by contract manufacturers to their upstream suppliers.

SONOS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(unaudited)

Legal proceedings

From time to time, the Company is involved in legal proceedings in the ordinary course of business, including claims relating to employee relations, business practices, and patent infringement. Litigation can be expensive and disruptive to normal business operations. Moreover, the results of complex legal proceedings are difficult to predict, and the Company's view of these matters may change in the future as the litigation and events related thereto unfold. The Company expenses legal fees as incurred. The Company records a provision for contingent losses when it is both probable that a liability will be incurred and the amount of the loss can be reasonably estimated. An unfavorable outcome to any legal matter, if material, could have an adverse effect on the Company's operations or its financial position, liquidity or results of operations.

The Company's Lawsuits Against Google:

On January 7, 2020, the Company filed a complaint with the U.S. International Trade Commission ("ITC") against Alphabet Inc. ("Alphabet") and Google LLC ("Google") and a counterpart lawsuit in the U.S. District Court for the Central District of California against Google. The complaint and lawsuit each allege infringement by Alphabet and Google of certain Sonos patents related to its smart speakers and related technology. The counterpart lawsuit is stayed pending completion of the ITC investigation and appeal thereof. The ITC concluded its investigation in January 2022, finding all five of the Company's asserted patents to be valid and infringed by Google, and further finding that one redesign per patent proposed by Google would avoid infringement. The ITC issued a limited exclusion order and a cease-and-desist order with respect to Google's infringing products. The outcome of the ITC investigation is currently being appealed by the Company and Google.

On September 29, 2020, the Company filed another lawsuit against Google alleging infringement of additional Sonos patents and seeking monetary damages and other non-monetary relief. This suit is pending in the U.S. District Court for the Northern District of California. In this lawsuit, Google has countersued the Company alleging breach of contract and conversion against the Company in connection with Google and the Company's collaboration in 2013. The Company disputes the claims and intends to defend these claims during the case. In this lawsuit, the judge has already concluded that Google infringes one asserted patent and that patent is not invalid. The judge has also ruled that another asserted patent is not infringed by Google and is invalid. This lawsuit is expected to be tried to a jury in May 2023.

On December 1, 2020, the Company filed a lawsuit against two Google foreign subsidiaries in the regional court of Hamburg, Germany, alleging infringement of a Sonos patent seeking non-monetary relief. The Company has since withdrawn this action after having received some preliminary relief.

Google's Lawsuits Against the Company:

On June 11, 2020, Google filed a lawsuit in the U.S. District Court for the Northern District of California against the Company alleging infringement by the Company of five Google patents and seeking monetary damages and other non-monetary relief. Four of these patents have since been found invalid by the court or by the U.S. Patent and Trademark Office, or have been withdrawn from the case by Google. In this lawsuit, one patent remains asserted against the Company. No trial date is set.

On June 12, 2020, Google filed lawsuits in District Court Munich I against Sonos Europe B.V. and Sonos, Inc., alleging infringement of two Google patents and seeking monetary damages and an injunction preventing sales of allegedly infringing products. In March 2021, the District Court Munich stayed the case for infringement of one Google patent pending the outcome of a nullity action concerning the validity of that patent. In June 2021, the Munich court issued a decision dismissing Google's complaint regarding the other Google patent for lack of infringement by the Company. Google has appealed the Munich court's ruling, which is pending.

SONOS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(unaudited)

On August 21, 2020, Google filed a lawsuit against the Company in Canada alleging infringement of one Google patent. On July 26, 2022, the Canadian court ruled that the Company does not infringe this patent after a trial on the merits. Google has appealed the Canadian court's ruling, which is pending.

On August 21, 2020, Google filed a lawsuit against Sonos Europe B.V. and Sonos, Inc. in France, alleging infringement of two Google patents and seeking monetary damages and an injunction preventing sales of allegedly infringing products. In February 2021, Google withdrew its infringement allegations regarding one patent in view of prior art brought to the attention of the court by the Company. In March 2022, the French trial court ruled for the Company on Google's other asserted patent. Google has appealed the French trial court's ruling, which is pending.

On August 21, 2020, Google filed a lawsuit against Sonos Europe B.V. and Sonos, Inc. in the Netherlands alleging infringement of a Google patent seeking an injunction preventing sales of allegedly infringing products. In October 2022, the Netherlands court ruled that the Company does not infringe Google's patent.

In September 2020, Google filed a lawsuit against Sonos Europe B.V. in the Netherlands, alleging infringement of a Google patent seeking an injunction preventing sales of allegedly infringing products. In February 2022, the Court rejected Google's claims concerning this patent. Google has appealed this decision, which is pending.

On August 8, 2022, Google filed two complaints with the ITC against the Company and two counterpart lawsuits in the Northern District of California against the Company, collectively alleging infringement by the Company of seven Google patents generally related to wireless charging, device setup, and voice control, and seeking monetary damages and other non-monetary relief. The ITC investigations are currently pending while the counterpart lawsuits are stayed pending completion of the ITC investigations. The ITC has terminated the investigation as to one Google patent as a result of imminent expiration of that Google patent. One of the two ITC investigations is scheduled for an oral hearing in June 2023 and scheduled for a final decision in January 2024, while the other of the two ITC investigations is scheduled for an oral hearing in July 2023 and scheduled for a final decision in May 2024. A range of loss, if any, associated with these matters is not probable or reasonably estimable as of December 31, 2022.

Implicit

On March 10, 2017, Implicit, LLC ("Implicit") filed a patent infringement action in the United States District Court, District of Delaware against the Company. Implicit is asserting that the Company infringed on two patents in this case. The Company denies the allegations. There is no assurance of a favorable outcome and the Company's business could be adversely affected as a result of a finding that the Company patents-in-suit are invalid and/or unenforceable. A range of loss, if any, associated with this matter is not probable or reasonably estimable as of December 31, 2022.

The Company is involved in certain other litigation matters not listed above but does not consider these matters to be material either individually or in the aggregate at this time. The Company's view of the matters not listed may change in the future as the litigation and events related thereto unfold.

Tariff refunds

On May 13, 2020, the Company was granted a temporary exclusion from the August 2019 Section 301 Tariff Action (List 4A) ("Section 301 tariffs"), eliminating the tariffs on the Company's component products imported from China until August 31, 2020. The exclusion for the Company's component products was not extended past August 31, 2020, with the Section 301 tariffs for our component products automatically reinstated on September 1, 2020. On July 23, 2020, the Company was granted a temporary exclusion from Section 301 tariffs, eliminating the tariffs on the Company's core speaker products imported from China until August 31, 2020. These exemptions entitled the Company to refunds for tariffs paid from September 2019 through December 2020. On August 28, 2020, the United States Trade Representative ("USTR") granted an extension through December 31, 2020, of the exclusion for the Company's core speaker products, with the Section 301 tariffs for our core speaker products automatically reinstated on January 1, 2021. On March 23, 2022, the Company was granted an exclusion extension from the

SONOS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(unaudited)

Section 301 tariffs, eliminating tariffs on the Company's core speaker products, including certain new product introductions, imported from China from April 13, 2022 through December 31, 2022. This exemption entitled the Company to refunds for tariffs paid from October 12, 2021 through April 12, 2022. On December 16, 2022, the USTR granted an extension through September 30, 2023, of the exclusion for the Company's core speaker products.

Tariff refund claims are subject to review and approval by the U.S. Customs and Border Protection. For the three months ended December 31, 2022, the Company recognized \$4.4 million in refunds based upon acceptance of the Company's refund request, recognized as a reduction to cost of revenue. As of December 31, 2022, the remaining refunds the Company expected to recover totaled approximately \$5.8 million, for tariffs paid from September 2019 through December 2020, and from October 12, 2021 through April 12, 2022. The Company did not record these potential refunds due to uncertainty of the timing of acceptance of approval, but such refunds will be recognized as a reduction to cost of revenue if and when acceptance occurs.

8. Stockholders' Equity

On November 16, 2022, the Board of Directors (the "Board") authorized a common stock repurchase program of up to \$100.0 million. During the three months ended December 31, 2022, the Company repurchased 849,806 shares for an aggregate purchase price of \$15.0 million at an average price of \$17.69 per share under the repurchase program. The Company had \$85.0 million available for share repurchases under the repurchase program as of December 31, 2022.

Treasury stock during the three months ended December 31, 2022, included shares withheld to satisfy employees' tax withholding requirements in connection with vesting of stock awards. Additionally, during the three months ended December 31, 2022, the Company retired 2,293,416 shares of treasury stock.

9. Stock-based Compensation

2018 Equity Incentive Plan

In July 2018, the Board adopted the 2018 Equity Incentive Plan (the "2018 Plan"). The 2018 Plan became effective in connection with the Company's initial public offering ("IPO"). The number of shares reserved for issuance under the 2018 Plan increases automatically on January 1 of each year beginning in 2019 and continuing through 2028 by a number of shares of common stock equal to the lesser of (x) 5% of the total outstanding shares of the Company's common stock and common stock equivalents as of the immediately preceding December 31 (rounded to the nearest whole share) and (y) a number of shares determined by the Company's Board.

Stock options

Pursuant to the 2018 Plan, the Company issues stock options to employees and directors. The option price, number of shares, and grant date are determined at the discretion of the Board. For so long as the option holder performs services for the Company, the options generally vest over 48 months, on a monthly or quarterly basis, with certain options subject to an initial annual cliff vest, and are exercisable for a period not to exceed ten years from the date of grant.

SONOS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(unaudited)

The summary of the Company's stock option activity is as follows:

	Number of Options	Weighted- Average Exercise Price	Weighted- Average Remaining Contractual Term (In years)	Aggregate Intrinsic Value (In thousands)
Outstanding at October 1, 2022	10,802,882	\$ 13.37	4.5	\$ 10,956
Exercised	(730,376)	11.10		
Forfeited	(20,943)	15.19		
Outstanding at December 31, 2022	10,051,563	\$ 13.53	4.2	\$ 33,834
At December 31, 2022				
Options exercisable	10,039,063	\$ 13.54	4.2	\$ 33,762
Options vested and expected to vest	10,051,332	\$ 13.53	4.2	\$ 33,833

As of December 31, 2022, and October 1, 2022, the Company had less than \$0.1 million and had \$0.4 million, respectively, of unrecognized stock-based compensation expense related to stock options, which are expected to be recognized over weighted-average periods of 0.1 and 0.2 years, respectively.

Restricted stock units ("RSU")

Pursuant to the 2018 Plan, the Company issues RSUs to employees and directors. RSUs vest quarterly over the service period, which is generally four years, with certain awards subject to an initial annual cliff vest. The summary of the Company's RSU activity is as follows:

	Number of Units	Weighted-Average Grant Date Fair Value	Aggregate Intrinsic Value (In thousands)
Outstanding at October 1, 2022	8,308,177	\$ 19.25	\$ 115,484
Granted	4,658,164	17.40	
Released	(992,867)	15.97	
Forfeited	(182,718)	18.95	
Outstanding at December 31, 2022	11,790,756	\$ 18.80	\$ 199,264
At December 31, 2022			
Units expected to vest	9,943,485	\$ 18.66	\$ 168,045

As of December 31, 2022, and October 1, 2022, the Company had \$166.6 million and \$120.6 million of unrecognized stock-based compensation expense related to RSUs, which are expected to be recognized over weighted-average periods of 2.8 and 2.5 years, respectively.

Performance stock units ("PSU")

Pursuant to the 2018 Plan, the Company has issued and may issue certain PSUs that vest on the satisfaction of service and performance conditions. The number of outstanding PSUs is based on the target number of share awards. The number of shares vested at the end of the performance period is based on achievement of performance conditions and may include adjustments to reflect the extent to which the corresponding performance goals have

SONOS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(unaudited)

been achieved. In the first quarter of fiscal 2023, the number of shares vested included performance achievement adjustments of a net reduction of 12,895 units. The summary of the Company's PSU activity is as follows:

	Number of Units	Weighted- Average Grant Date Fair Value	Aggregate Intrinsic Value (In thousands)
Outstanding at October 1, 2022	398,077	\$ 26.96	\$ 5,533
Granted	249,370	17.54	
Vested	(263,158)	26.26	
Outstanding at December 31, 2022	<u>384,289</u>	\$ 21.33	\$ 6,494

As of December 31, 2022, and October 1, 2022, the Company had \$3.5 million and \$0.4 million of unrecognized stock-based compensation expense related to PSUs, which are expected to be recognized over weighted-average periods of 2.0 and 0.6 years, respectively.

Stock-based compensation

Total stock-based compensation expense by functional category was as follows:

	Three Months Ended December 31, 2022	January 1, 2022
(In thousands)		
Cost of revenue	\$ 570	\$ 328
Research and development	9,151	6,738
Sales and marketing	4,113	3,647
General and administrative	6,361	6,746
Total stock-based compensation expense	<u>\$ 20,195</u>	<u>\$ 17,459</u>

10. Income Taxes

The Company's tax provision and the resulting effective tax rate for interim periods is determined based upon its estimated annual effective tax rate ("AETR"), adjusted for the effect of discrete items arising in that quarter. The impact of such inclusions could result in a higher or lower effective tax rate during a quarter, based upon the mix and timing of actual earnings or losses versus annual projections. In each quarter, the Company updates its estimate of the AETR, and if the estimated AETR changes, a cumulative adjustment is made in that quarter.

The Company recorded a provision for income taxes of \$36.5 million and \$7.6 million for the three months ended December 31, 2022, and January 1, 2022, respectively, related to U.S. and non-U.S. income taxes. For the three months ended December 31, 2022, the Company's tax expense increased significantly when compared to the three months ended January 1, 2022, primarily due to the requirement to capitalize and amortize research and development expenses under Section 174 of the U.S. Internal Revenue Code ("Section 174") effective the quarter ended December 31, 2022. This resulted in the Company recording significant U.S. current tax expense and no corresponding deferred tax benefit due to the valuation allowance maintained against its U.S. deferred tax assets. For the three months ended January 1, 2022, the Company excluded certain foreign jurisdictions from the calculation of the AETR as the Company anticipated an overall ordinary loss for which no tax benefit could be recognized. For the three months ended January 1, 2022, the Company's tax provision included a discrete income tax benefit of \$3.2 million for the release of a portion of the Company's U.S. valuation allowance because of an acquisition in the quarter and U.S. share-based compensation.

For the three months ended December 31, 2022, the Company maintained a full valuation allowance on its deferred tax assets in the U.S. and certain other non-US entities due to a history of operating losses. It is possible

SONOS, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (CONTINUED)
(unaudited)

that within the next 12 months there may be sufficient positive evidence to release a portion or all of the valuation allowance. Release of the valuation allowance in the U.S. and certain other non-US entities would result in a benefit to income tax expense for the period the release is recorded, which could have a material impact on net earnings. The timing and amount of the potential valuation allowance release are subject to significant management judgment, as well as prospective earnings in the U.S. and certain other non-US entities.

11. Net Income Per Share Attributable to Common Stockholders

Basic net income per share attributable to common stockholders is calculated by dividing net income attributable to common stockholders by the weighted-average number of shares of common stock outstanding less shares subject to repurchase. Diluted net income per share attributable to common stockholders adjusts the basic net income per share attributable to common stockholders and the weighted-average number of shares of common stock outstanding for the potentially dilutive impact of stock awards, using the treasury stock method.

The following table sets forth the computation of the Company's basic and diluted net income per share attributable to common stockholders:

	Three Months Ended	
	December 31, 2022	January 1, 2022
(In thousands, except share and per share data)		
Numerator:		
Net income attributable to common stockholders - basic and diluted	\$ 75,188	\$ 123,481
Denominator:		
Weighted-average shares of common stock—basic	127,212,245	127,662,826
Effect of potentially dilutive stock options	1,802,786	8,162,237
Effect of RSUs	2,460,948	6,306,547
Effect of PSUs	27,007	190,838
Weighted-average shares of common stock—diluted	<u>131,502,986</u>	<u>142,322,448</u>
Net income per share attributable to common stockholders:		
Basic	\$ 0.59	\$ 0.97
Diluted	\$ 0.57	\$ 0.87

The following potentially dilutive shares were excluded from the computation of diluted net income per share attributable to common stockholders because including them would have been antidilutive:

	Three Months Ended	
	December 31, 2022	January 1, 2022
Stock options to purchase common stock	8,624,436	5,838,942
Restricted stock units	7,664,566	3,529,909
Performance stock units	61,681	110,669
Total	<u>16,350,683</u>	<u>9,479,520</u>

12. Retirement Plans

The Company has a defined contribution 401(k) plan (the "401(k) Plan") for the Company's U.S.-based employees, as well as various defined contribution plans for its international employees. Eligible U.S. employees may make tax-deferred contributions under the 401(k) plan but are limited to the maximum annual dollar amount allowable under the Internal Revenue Code of 1986, as amended (the "Code"). The Company matches contributions towards the 401(k) Plan and international defined contribution plans. The Company's matching contributions totaled \$2.3 million and \$1.9 million for the three months ended December 31, 2022, and January 1, 2022, respectively.

Item 2. Management's discussion and analysis of financial condition and results of operations

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our condensed consolidated financial statements and related notes included in Part I, Item 1 of this Quarterly Report on Form 10-Q and with our audited consolidated financial statements included in our Annual Report.

We operate on a 52- week or 53- week fiscal year ending on the Saturday nearest September 30 each year. Our fiscal year is divided into four quarters of 13 weeks, each beginning on a Sunday and containing two 4-week periods followed by a 5-week period. An additional week is included in the fourth fiscal quarter approximately every five years to realign fiscal quarters with calendar quarters.

Forward-Looking Statements

This Quarterly Report on Form 10-Q contains forward-looking statements. All statements other than statements of historical facts contained in this Quarterly Report on Form 10-Q, including statements regarding future operations, are forward-looking statements. In some cases, forward-looking statements may be identified by words such as “believe,” “may,” “will,” “estimate,” “continue,” “anticipate,” “intend,” “could,” “would,” “expect,” “objective,” “plan,” “potential,” “seek,” “grow,” “target,” “if,” and similar expressions intended to identify forward-looking statements. We have based these forward-looking statements largely on our current expectations and projections about future events and trends that we believe may affect our financial condition, results of operations, business strategy, short-term and long-term business operations, objectives and financial needs. These forward-looking statements are subject to a number of risks, uncertainties and assumptions, including those described in the section titled “Risk Factors” set forth in Part II, Item 1A of this Quarterly Report on Form 10-Q and in our other SEC filings, including our Annual Report. Moreover, we operate in a very competitive and rapidly changing environment. New risks emerge from time to time. It is not possible for our management to predict all risks, nor can we assess the impact of all factors on our business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements we may make. In light of these risks, uncertainties and assumptions, the future events and trends discussed in this Quarterly Report on Form 10-Q may not occur and actual results may differ materially and adversely from those anticipated or implied in the forward-looking statements. You should read this Quarterly Report on Form 10-Q with the understanding that our actual future results, levels of activity, performance and events and circumstances may be materially different from what we expect. Except as required by law, we do not undertake any obligation to publicly update any forward-looking statements, whether as a result of new information, future developments or otherwise.

Overview

Sonos is one of the world's leading sound experience brands.

We pioneered multi-room, wireless audio products, debuting the world's first multi-room wireless sound system in 2005. Today, our products include wireless, portable, home theater speakers, components, and accessories to address consumers' evolving audio needs. We are known for delivering unparalleled sound, thoughtful design aesthetic, simplicity of use, and an open platform. Our platform has attracted a broad range of more than 130 streaming content providers, such as Apple Music, Spotify, Deezer, and Pandora. These partners find value in our independent platform and access to our millions of desirable and engaged customers. We frequently introduce new services and features across our platform, providing our customers with enhanced functionality, improved sound, and an enriched user experience. We are committed to continuous technological innovation as reflected in our growing global patent portfolio. We believe our patents comprise the foundational intellectual property for wireless multi-room and other audio technologies.

Our innovative products, seamless customer experience, and expanding global footprint have driven 17 consecutive years of sustained revenue growth since our first product launch. We generate revenue from sales of our Sonos speaker products, including wireless speakers and home theater speakers, Sonos system products, which largely comprises our component products, and partner products and other revenue, including partnerships with IKEA and Sonance, Sonos and third-party accessories, licensing, advertising, and subscription revenue.

We have developed a robust product and software roadmap that we believe will help us capture the expanding addressable market for our products. We believe executing on our roadmap will position us to acquire new customers, offer a continuously improving experience to our existing customers, and grow follow-on purchases.

Recent Developments

While the effects of the COVID-19 pandemic persist, the impacts are abating. During our first quarter of fiscal 2023, we saw recovery in supply for our products. For certain products that had been supply constrained through the fourth quarter of fiscal 2022, we increased our investments in inventory components in the first quarter of fiscal 2023, compared to the first quarter of fiscal 2022, resulting in successful recovery of supply of those products. We also saw improvements within our supply chain including lower shipping and logistics costs, as well as shortening lead times. Additionally, we shifted more production into our new contract manufacturing locations in Malaysia and Vietnam, resulting in savings from tariff avoidance.

The economic environment during our first quarter of fiscal 2023 was affected by challenging macroeconomic trends including inflation, rising interest rates, recessionary concerns, volatility in foreign exchange rates, as well as continuing conflict between Russia and Ukraine. Our revenue and gross margin were negatively impacted by unfavorable foreign exchange rates for the first quarter of fiscal 2023 compared to the first quarter of fiscal 2022.

While these events are unusual and dynamic, we have considered their impacts based on information currently available when developing our estimates and assumptions. Actual results and outcomes may differ from our estimates and assumptions. For additional information of risks related to COVID-19 and economic and political uncertainty, refer to Part II, Item 1A. Risk factors.

Key Metrics

In addition to the measures presented in our condensed consolidated financial statements, we use the following key metrics to evaluate our business, measure our performance, identify trends affecting our business and assist us in making strategic decisions. Our key metrics are total revenue, products sold, adjusted EBITDA and adjusted EBITDA margin. The most directly comparable financial measure calculated under U.S. GAAP for adjusted EBITDA is net income (loss). In the three months ended December 31, 2022, and January 1, 2022, we had net income of \$75.2 million and \$123.5 million, respectively.

	Three Months Ended	
	December 31, 2022	January 1, 2022
(In thousands, except percentages)		
Total revenue	\$ 672,579	\$ 664,481
Products sold	2,482	2,398
Adjusted EBITDA ⁽¹⁾	\$ 123,920	\$ 163,143
Adjusted EBITDA margin ⁽¹⁾	18.4%	24.6%

- (1) For additional information regarding adjusted EBITDA and adjusted EBITDA margin (which are non-GAAP financial measures), including reconciliations of net income (loss), to adjusted EBITDA, see the sections titled "Adjusted EBITDA and Adjusted EBITDA Margin" and "Non-GAAP Financial Measures" below.

Products Sold

Products sold represents the number of products that are sold during a period, net of returns and includes the sale of products in the Sonos speakers and Sonos system products categories, as well as module units sold through our partnerships with IKEA and Sonance from our Partner products and other revenue category. Growth rates between products sold and revenue are not perfectly correlated because our revenue is affected by other variables, such as the mix of products sold during the period, promotional discount activity, the introduction of new products that may have higher or lower than average selling prices, as well as the impact of recognition of previously deferred revenue.

Adjusted EBITDA and Adjusted EBITDA Margin

We define adjusted EBITDA as net income (loss) adjusted to exclude the impact of stock-based compensation expense, depreciation and amortization, interest, other income (expense), taxes, and other items that we do not consider representative of our underlying operating performance.

We define adjusted EBITDA margin as adjusted EBITDA divided by revenue. See "Non-GAAP Financial Measures" below for information regarding our use of adjusted EBITDA and adjusted EBITDA margin, and a reconciliation of net income (loss) to adjusted EBITDA.

Non-GAAP Financial Measures

To supplement our condensed consolidated financial statements presented in accordance with U.S. GAAP, we monitor and consider adjusted EBITDA and adjusted EBITDA margin, which are non-GAAP financial measures. These non-GAAP financial measures are not based on any standardized methodology prescribed by U.S. GAAP and are not necessarily comparable to similarly titled measures presented by other companies.

We define adjusted EBITDA as net income (loss) adjusted to exclude the impact of depreciation and amortization, stock-based compensation expense, interest income, interest expense, other income (expense), income taxes, and other items that we do not consider representative of underlying operating performance. We define adjusted EBITDA margin as adjusted EBITDA divided by revenue.

We use these non-GAAP financial measures to evaluate our operating performance and trends and make planning decisions. We believe that these non-GAAP financial measures help identify underlying trends in our business that could otherwise be masked by the effect of the expenses and other items that we exclude from these non-GAAP financial measures. Accordingly, we believe that these non-GAAP financial measures provide useful information to investors and others in understanding and evaluating our operating results, enhancing the overall understanding of our past performance and future prospects, and allowing for greater transparency with respect to a key financial metric used by our management in its financial and operational decision-making.

Adjusted EBITDA and adjusted EBITDA margin are non-GAAP financial measures, and should not be considered in isolation of, or as an alternative to, measures prepared in accordance with U.S. GAAP. There are a number of limitations related to the use of adjusted EBITDA rather than net income (loss), which is the nearest U.S. GAAP equivalent to adjusted EBITDA, and the use of adjusted EBITDA margin rather than operating margin, which is the nearest U.S. GAAP equivalent to adjusted EBITDA margin. These limitations include that the non-GAAP financial measures:

- exclude depreciation and amortization, and although these are non-cash expenses, the assets being depreciated may be replaced in the future;
- exclude stock-based compensation expense, which has been, and will continue to be, a significant recurring expense for our business and an important part of our compensation strategy;
- do not reflect interest income, primarily resulting from interest income earned on our cash and cash equivalent balances;
- do not reflect interest expense, or the cash requirements necessary to service interest or principal payments on our debt, which reduces cash available to us;
- do not reflect the effect of foreign currency exchange gains or losses, which is included in other income (expense), net;
- do not reflect the provision for or benefit from income tax that may result in payments that reduce cash available to us;
- do not reflect items that are not considered representative of our underlying operating performance which reduce cash available to us; and
- may not be comparable to similar non-GAAP financial measures used by other companies, because the expenses and other items that we exclude in our calculation of these non-GAAP financial measures may differ from the expenses and other items, if any, that other companies may exclude from these non-GAAP financial measures when they report their operating results.

Because of these limitations, these non-GAAP financial measures should be considered along with other operating and financial performance measures presented in accordance with U.S. GAAP.

The following table presents a reconciliation of net income to adjusted EBITDA:

	Three Months Ended	
	December 31, 2022	January 1, 2022
(In thousands, except percentages)		
Net income	\$ 75,188	\$ 123,481
Add (deduct):		
Depreciation and amortization	11,132	9,217
Stock-based compensation expense	20,195	17,459
Interest income	(1,967)	(33)
Interest expense	158	98
Other income (expense), net	(23,576)	1,402
Provision for income taxes	36,501	7,646
Legal and transaction related costs ⁽¹⁾	6,289	3,873
Adjusted EBITDA	\$ 123,920	\$ 163,143
Revenue	\$ 672,579	\$ 664,481
Adjusted EBITDA margin	18.4%	24.6%

⁽¹⁾ Legal and transaction-related costs consist of expenses related to our intellectual property ("IP") litigation against Alphabet and Google, as well as legal and transaction costs associated with our acquisition activity, which we do not consider representative of our underlying operating performance.

Factors Affecting Performance

New product introductions. Since 2005, we have released products in multiple audio categories. We intend to introduce new products that appeal to a broad set of consumers, as well as bring our differentiated listening platform and experience to all the places and spaces where our customers listen to the breadth of audio content available, including inside and outside their homes.

Seasonality. Historically, we have typically experienced the highest levels of revenue in the first fiscal quarter of the year coinciding with the holiday shopping season and our promotional activities. Our promotional discounting activity is typically higher in the first fiscal quarter as well, which negatively impacts gross margin during this period. However, our higher sales volume in the holiday shopping season has historically resulted in a higher operating margin in the first fiscal quarter due to positive operating leverage.

Ability to Sell Additional Products to Existing Customers. Our existing customers typically increase the number of Sonos products in their homes. As we execute on our product roadmap to address evolving consumer preferences, we believe we can expand the number of products in our customers' homes. Our ability to sell additional products to existing customers is a key part of our business model, as follow-on purchases indicate high customer engagement and satisfaction, decrease the likelihood of competitive substitution, and result in higher customer lifetime value. We will continue to innovate and invest in product development in order to enhance customer experience and drive sales of additional products to existing customers.

Channel strategy. We believe growing our own e-commerce channel will continue to be important to supporting our overall growth and profitability as consumers continue the shift from physical to online sales channels. We are investing in our e-commerce capabilities and in-app experience to drive direct sales.

While we seek to increase sales through our direct-to-consumer sales channel, we expect that our partnerships with third-party retailers and custom installers will continue to be an important part of our ecosystem. We will continue to seek retail partners that can deliver differentiated in-store experiences to support customer demand for product demonstrations. Additionally, we intend to expand and strengthen our partnerships with custom installers who are valuable to our customer base and contribute to our new household growth. Our physical retail distribution relies on third-party retailers and our ability to maintain our diversified manufacturing footprint and base of component suppliers in support of production efficiency and flexibility across our global supply chain.

For additional information regarding factors affecting performance, refer to Risk factors in Part II, Item 1A. of this Quarterly Report on Form 10-Q, Part I, Item 1. "Business - Factors Affecting Performance" of our Annual Report, and the Risk factors in Part I, Item 1A. of our Annual Report.

Components of Results of Operations

Revenue

We generate substantially all of our revenue from the sale of Sonos speakers and Sonos system products. We also generate a portion of revenue from Partner products and other revenue sources, such as module revenue from our IKEA partnership, architectural speakers from our Sonance partnership, and accessories such as speaker stands and wall mounts, as well as professional services, licensing, advertising, and subscription revenue. We attribute revenue from our IKEA partnership to our Asia Pacific ("APAC") region, as our regional revenue is defined by the shipment location. Our revenue is recognized net of allowances for returns, discounts, sales incentives, and any taxes collected from customers. We also defer a portion of our revenue that is allocated to unspecified software upgrades and cloud-based services, as well as for newly launched products sold to resellers not recognized until the date of general availability is reached. Our revenue is subject to fluctuation based on the foreign currency in which our products are sold, principally for sales denominated in the euro and the British pound. The introduction of new products may result in an increase in revenue but may also impact revenue generated from existing products as consumers shift purchases to new products.

Cost of Revenue

Cost of revenue consists of product costs, including costs of our contract manufacturers for production, components, shipping and handling, tariffs, duty costs, warranty replacement costs, packaging, fulfillment costs, manufacturing and tooling equipment depreciation, warehousing costs, hosting costs, and excess and obsolete inventory write-downs. It also includes licensing costs, such as royalties to third parties, and attributable amortization of acquired developed technology. In addition, we allocate certain costs related to management and facilities, personnel-related expenses, and supply chain logistic costs. Personnel-related expenses consist of salaries, bonuses, benefits, and stock-based compensation expenses.

Gross Profit and Gross Margin

Our gross margin has fluctuated and may, in the future, fluctuate from period to period based on a number of factors, including the mix of products we sell, the channel mix through which we sell our products, fluctuations of the impacts of our product and material cost saving initiatives, the foreign currency in which our products are sold, and tariffs and duty costs implemented by governmental authorities.

Operating Expenses

Operating expenses consist of research and development, sales and marketing, and general and administrative expenses.

Research and development. Research and development expenses consist primarily of personnel-related expenses, consulting and contractor expenses, tooling, test equipment, prototype materials, and related overhead costs. To date, software development costs have been expensed as incurred because the period between achieving technological feasibility and the release of the software has been short and development costs qualifying for capitalization have been insignificant.

Sales and marketing. Sales and marketing expenses consist primarily of advertising and marketing activity for our products and personnel-related expenses, as well as trade show and event costs, sponsorship costs, consulting and contractor expenses, travel costs, depreciation for product displays, as well as related maintenance and repair expenses, customer experience and technology support tool expenses, revenue related sales fees from our direct-to-consumer business, and overhead costs.

General and administrative. General and administrative expenses consist of personnel-related expenses for our finance, legal, human resources and administrative personnel, as well as the costs of professional services, information technology, litigation, patents, related overhead, and other administrative expenses.

Other Income (Expense), Net

Interest income. Interest income consists primarily of interest income earned on our cash and cash equivalents balances.

Interest expense. Interest expense consists primarily of interest expense associated with our debt financing arrangements and amortization of debt issuance costs.

Other income (expense), net. Other income (expense), net consists primarily of our foreign currency exchange gains and losses relating to transactions and remeasurement of asset and liability balances denominated in currencies other than the U.S. dollar. We expect our foreign currency gains and losses to continue to fluctuate in the future due to changes in foreign currency exchange rates.

Provision for Income Taxes

We are subject to income taxes in the United States and foreign jurisdictions in which we operate. Foreign jurisdictions have statutory tax rates different from those in the United States. Accordingly, our effective tax rate will vary depending on jurisdictional mix of earnings, and changes in tax laws. In addition, certain U.S. tax regulations subject the earnings of our non-U.S. subsidiaries to current taxation in the United States. Our effective tax rate will be impacted by our ability to claim deductions and foreign tax credits to offset the taxation of foreign earnings in the United States.

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. A valuation allowance is provided to reduce our deferred tax assets to amounts that are more-likely-than-not to be realized. We have assessed, on a jurisdictional basis, the available means of recovering deferred tax assets, including the ability to carry back net operating losses, the existence of taxable temporary differences, the availability of tax planning strategies and available sources of future taxable income. We have concluded that a valuation allowance on deferred tax assets in the U.S. continues to be appropriate considering cumulative pre-tax losses in recent years and uncertainty with respect to future taxable income.

It is possible that within the foreseeable future there may be sufficient positive evidence to release a portion or all of the remaining valuation allowance. Release of the remaining valuation allowance would result in a benefit to income tax expense for the period the release is recorded, which could have a material impact on net earnings. The timing and amount of the potential valuation allowance release are subject to significant management judgment, as well as prospective earnings in the United States.

Results of Operations

The following table sets forth our condensed consolidated results of operations for the periods indicated. The period-to-period comparison of financial results is not necessarily indicative of financial results to be achieved in future periods.

(Dollars in thousands)	Three Months Ended			
	December 31, 2022		January 1, 2022	
	\$	%	\$	%
Revenue	\$ 672,579	100.0%	\$ 664,481	100.0%
Cost of revenue ⁽¹⁾	387,522	57.6	347,096	52.2
Gross profit	285,057	42.4	317,385	47.8
Operating expenses				
Research and development ⁽¹⁾	76,940	11.4	61,330	9.2
Sales and marketing ⁽¹⁾	78,696	11.7	83,736	12.6
General and administrative ⁽¹⁾	43,117	6.4	39,725	6.0
Total operating expenses	198,753	29.6	184,791	27.8
Operating income	86,304	12.8	132,594	20.0
Other income (expense), net				
Interest income	1,967	0.3	33	—
Interest expense	(158)	—	(98)	—
Other income (expense), net	23,576	3.5	(1,402)	(0.2)
Total other income (expense), net	25,385	3.8	(1,467)	(0.2)
Income before provision for income taxes	111,689	16.6	131,127	19.7
Provision for income taxes	36,501	5.4	7,646	1.2
Net income	\$ 75,188	11.2%	\$ 123,481	18.6%
Adjusted EBITDA ⁽²⁾	\$ 123,920	18.4%	\$ 163,143	24.6%

⁽¹⁾ Amounts include stock-based compensation expense as follows:

(In thousands, except percentages)	Three Months Ended			
	December 31, 2022		January 1, 2022	
	\$	%	\$	%
Cost of revenue	\$ 570	0.1%	\$ 328	—
Research and development	9,151	1.4	6,738	1.0
Sales and marketing	4,113	0.6	3,647	0.5
General and administrative	6,361	0.9	6,746	1.0
Total stock-based compensation expense	\$ 20,195	3.0%	\$ 17,459	2.6%

⁽²⁾ Adjusted EBITDA is a financial measure that is not calculated in accordance with U.S. GAAP. See the sections titled “Adjusted EBITDA and adjusted EBITDA margin” and “Non-GAAP financial measures” above.

Comparison of the three months ended December 31, 2022, and January 1, 2022

Revenue

Comparison of the three months ended December 31, 2022, and January 1, 2022

(In thousands, except percentages)	Three Months Ended		Change	
	December 31, 2022	January 1, 2022	\$	%
Sonos speakers	\$ 539,196	\$ 501,886	\$ 37,310	7.4%
Sonos system products	114,434	134,745	(20,311)	(15.1)
Partner products and other revenue	18,949	27,850	(8,901)	(32.0)
Total revenue	\$ 672,579	\$ 664,481	\$ 8,098	1.2%

Total revenue increased 1.2% for the three months ended December 31, 2022, compared to the three months ended January 1, 2022. The growth was mainly driven by higher volume resulting from higher promotional activity, and availability of supply, offset by unfavorable foreign exchange rates.

Sonos speakers revenue represented 80.2% of total revenue for the three months ended December 31, 2022. The category increased 7.4% compared to the three months ended January 1, 2022, driven by the introduction of Sub mini, and the continued success of Arc, partially offset by decreased sales in Roam and Beam. Sonos system products represented 17.0% of total revenue for the three months ended December 31, 2022, and decreased 15.1% compared to the three months ended January 1, 2022, due to the increase in the prior year related to significant inventory replenishment following significant supply chain constraints. Partner products and other revenue represented 2.8% of total revenue for the three months ended December 31, 2022, and decreased 32.0% compared to the three months ended January 1, 2022, primarily driven by a decrease in orders of our partner products.

Revenue for the three months ended December 31, 2022, compared to the three months ended January 1, 2022, increased 6.1% in the Americas, decreased 2.1% in EMEA, and increased 11.1% on a constant currency basis, and decreased 21.3% in APAC, and decreased 14.9% on a constant currency basis.

In constant currency U.S. dollars, total revenue increased 7.0% for the three months ended December 31, 2022, compared to the three months ended January 1, 2022. Beginning in the first quarter of fiscal 2023, we began calculating constant currency growth percentages by translating our current period financial results using the prior period average currency exchange rates and comparing these amounts to our prior period reported results.

	Three Months Ended		Change	
	December 31, 2022	January 1, 2022		
(Units in thousands)				
Total products sold	2,482	2,398	84	3.5%

The volume of products sold increased 3.5% for the three months ended December 31, 2022, compared to the three months ended January 1, 2022, mainly driven by an increase in the Sonos speakers category, offset by declines in partner products and other revenue, and Sonos system products. The rates of increase of volume of products sold and revenue differed for the three months ended December 31, 2022, primarily due to the impact of product mix, offset by promotional activity, as well as the impact of foreign exchange rates.

Cost of Revenue and Gross Profit

Comparison of the three months ended December 31, 2022, and January 1, 2022

	Three Months Ended		Change	
	December 31, 2022	January 1, 2022	\$	%
(In thousands, except percentages)				
Cost of revenue	\$ 387,522	\$ 347,096	\$ 40,426	11.6%
Gross profit	\$ 285,057	\$ 317,385	\$ (32,328)	(10.2)%
Gross margin	42.4%	47.8%		

Cost of revenue increased \$40.4 million, or 11.6%, to \$387.5 million for the three months ended December 31, 2022, compared to \$347.1 million for the three months ended January 1, 2022, primarily due to the increase in products sold, as well as higher component costs, partially offset by lower air freight shipping costs.

Gross margin decreased 540 basis points for the three months ended December 31, 2022, compared to the three months ended January 1, 2022. The decrease was primarily due to higher promotional activity, as well as higher component costs, and the impact of unfavorable foreign exchange rates. The decrease was partially offset by lower air freight shipping costs, and a reduction in tariff expenses of \$8.9 million, net of refunds recognized, resulting from an extension of our exemption from tariffs on core speaker products, which we did not have in the first quarter of fiscal 2022. Additionally, we benefited from tariff avoidance as a result of our diversification of production in Malaysia and Vietnam.

Research and Development

Comparison of the three months ended December 31, 2022, and January 1, 2022

	Three Months Ended		Change	
	December 31, 2022	January 1, 2022	\$	%
(In thousands, except percentages)				
Research and development	\$ 76,940	\$ 61,330	\$ 15,610	25.5%
Percentage of revenue	11.4%	9.2%		

Research and development expenses increased \$15.6 million, or 25.5%, for the three months ended December 31, 2022, compared to the three months ended January 1, 2022. This increase was primarily driven by \$13.1 million of higher personnel-related expenses and stock-based compensation driven by increased headcount, and an increase of \$1.6 million in product development costs.

Sales and Marketing

Comparison of the three months ended December 31, 2022, and January 1, 2022

	Three Months Ended		Change	
	December 31, 2022	January 1, 2022	\$	%
(In thousands, except percentages)				
Sales and marketing	\$ 78,696	\$ 83,736	\$ (5,040)	(6.0)%
Percentage of revenue	11.7%	12.6%		

Sales and marketing expenses decreased \$5.0 million, or 6.0%, for the three months ended December 31, 2022, compared to the three months ended January 1, 2022. This decrease was primarily driven by lower marketing expenses of \$8.3 million, partially offset by an increase of \$1.4 million in personnel-related expenses and stock-based compensation, as well as an increase of \$1.3 million in revenue-related sales fees from higher sales in our direct-to-consumer business.

General and Administrative

Comparison of the three months ended December 31, 2022, and January 1, 2022

	Three Months Ended		Change	
	December 31, 2022	January 1, 2022	\$	%
(In thousands, except percentages)				
General and administrative	\$ 43,117	\$ 39,725	\$ 3,392	8.5%
Percentage of revenue	6.4%	6.0%		

General and administrative expenses increased \$3.4 million, or 8.5%, for the three months ended December 31, 2022, compared to the three months ended January 1, 2022. The increase was primarily driven by \$2.0 million in personnel-related expenses due to increased headcount, as well as by \$1.7 million in higher legal fees, including legal fees incurred in connection with our IP litigation. The increase was partially offset by a \$0.7 million decrease for investments in information technology in fiscal 2022 that did not recur in the three months ended December 31, 2022, including replacing our legacy enterprise resource planning system, net of amortization of capitalizable implementation costs.

Interest Income, Interest Expense and Other Income (Expense), Net

Comparison of the three months ended December 31, 2022, and January 1, 2022

	Three Months Ended		Change	
	December 31, 2022	January 1, 2022	\$	%
(In thousands, except percentages)				
Other income (expense), net				
Interest income	\$ 1,967	\$ 33	\$ 1,934	*
Interest expense	(158)	(98)	(60)	61.2%
Other income (expense), net	23,576	(1,402)	24,978	*
Total other income (expense), net	<u>\$ 25,385</u>	<u>\$ (1,467)</u>	<u>\$ 26,852</u>	<u>*</u>

*not meaningful

Interest income for the three months ended December 31, 2022 compared to the three months ended January 1, 2022 increased due to higher yields on our cash and cash equivalents. Interest expense for the three months ended December 31, 2022 compared to the three months ended January 1, 2022 increased primarily due to expenses associated with our Revolving Credit Agreement. The increase in other income or expense, net for the three months ended December 31, 2022 compared to the three months ended January 1, 2022 was due to foreign currency exchange gains.

Provision for Income Taxes

Comparison of the three months ended December 31, 2022, and January 1, 2022

	Three Months Ended		Change	
	December 31, 2022	January 1, 2022	\$	%
(In thousands, except percentages)				
Provision for income taxes	\$ 36,501	\$ 7,646	\$ 28,855	*

*not meaningful

The provision for income taxes increased from \$7.6 million for the three months ended January 1, 2022, to \$36.5 million for the three months ended December 31, 2022.

For the three months ended December 31, 2022, our tax expense increased significantly when compared to the three months ended January 1, 2022, primarily due to the requirement to capitalize and amortize research and development expenses under Section 174 of the U.S. Internal Revenue Code ("Section 174") effective the quarter ended December 31, 2022. As a result, we recorded significant U.S. current tax expense and no corresponding deferred tax benefit due to the valuation allowance maintained against our U.S. deferred tax assets.

For the three months ended January 1, 2022, our tax provision included a discrete benefit of \$3.2 million for the release of a portion of our U.S. valuation allowance because of an acquisition in the quarter and U.S. share-based compensation.

Liquidity and Capital Resources

Our operations are financed primarily through cash flows from operating activities and net proceeds from the sale of our equity securities. As of December 31, 2022, our principal sources of liquidity consisted of cash flows from operating activities, cash and cash equivalents of \$431.5 million, including \$71.1 million held by our foreign subsidiaries, proceeds from the exercise of stock options and borrowing capacity under the credit facility under our Revolving Credit Agreement. In accordance with our policy, the undistributed earnings of our non-U.S. subsidiaries remain indefinitely reinvested outside of the United States as of December 31, 2022, as they are required to fund needs outside of the United States. In the event funds from foreign operations are needed to fund operations in the

United States and if U.S. tax has not already been previously provided, we may be required to accrue and pay additional U.S. taxes to repatriate these funds.

We believe our existing cash and cash equivalent balances, cash flows from operations and committed credit lines will be sufficient to meet our long-term working capital and capital expenditure needs for at least the next 12 months. In October 2021, we entered into a Revolving Credit Agreement with JPMorgan Chase Bank, N.A., as the administrative agent, Bank of America N.A., Morgan Stanley Senior Funding, Inc., and Goldman Sachs Bank USA, which allows us to borrow up to \$100.0 million, with a maturity date of October 2026. Our future capital requirements may vary materially from those currently planned and will depend on many factors, including our rate of revenue growth, the timing and extent of spending on research and development efforts and other business initiatives, our planned sales and marketing activities, the timing of new product introductions, our potential merger and acquisition activity, market acceptance of our products, and overall economic conditions. To the extent that current and anticipated sources of liquidity are insufficient to fund our future business activities and requirements, we may be required to seek additional equity or debt financing. The sale of additional equity would result in increased dilution to our stockholders. If we were to incur additional debt financing it would result in increased debt service obligations and the instruments governing such debt could provide for operating and financing covenants that would restrict our operations.

Debt Obligations

On October 13, 2021, we entered into the Revolving Credit Agreement. The Revolving Credit Agreement provides for (i) a five-year senior secured revolving credit facility in the amount of up to \$100.0 million and (ii) an uncommitted incremental facility subject to certain conditions. Proceeds are to be used for working capital and general corporate purposes. The facility may be drawn as an Alternative Base Rate Loan (at 1.00% plus an applicable margin) or Eurocurrency Loans (at the London interbank offered rate ("LIBOR") plus an applicable margin). We must also pay (i) an unused commitment fee ranging from 0.200% to 0.275% per annum of the average daily unused portion of the aggregate revolving credit commitment under the agreement and (ii) a per annum fee equal to the applicable margin over LIBOR multiplied by the aggregate face amount of outstanding letters of credit. As of December 31, 2022, we did not have any outstanding borrowings and had \$3.0 million in undrawn letters of credit that reduce the availability under the Revolving Credit Agreement.

Our obligations under the Revolving Credit Agreement are secured by substantially all of our assets. The Revolving Credit Agreement contains customary representations and warranties, customary affirmative and negative covenants, a financial covenant that is tested quarterly and requires us to maintain a certain consolidated leverage ratio, and customary events of default. As of December 31, 2022, we were in compliance with all financial covenants under the Revolving Credit Agreement.

Cash Flows

The following table summarizes our cash flows for the periods indicated:

	Three Months Ended	
	December 31, 2022	January 1, 2022
(In thousands)		
Net cash provided by (used in):		
Operating activities	\$ 182,286	\$ 179,934
Investing activities	(14,689)	(33,456)
Financing activities	(15,316)	(30,944)
Effect of exchange rate changes	4,397	(1,218)
Net increase in cash, cash equivalents and restricted cash	<u>\$ 156,678</u>	<u>\$ 114,316</u>

Cash flows from operating activities

Net cash provided by operating activities of \$182.3 million for the three months ended December 31, 2022, consisted of net income of \$75.2 million, non-cash adjustments of \$20.6 million, and a net increase in cash related

to changes in operating assets and liabilities of \$86.5 million. Non-cash adjustments primarily consisted of stock-based compensation expense of \$20.2 million, depreciation and amortization of \$11.1 million, and other non-cash adjustments, offset by a foreign currency exchange gain of \$17.7 million. The net increase in cash related to operating assets and liabilities was primarily due to a decrease in inventories of \$143.1 million due to the seasonality of our business with higher sales during the holiday season, as well as higher promotional activity, an increase in other liabilities of \$15.8 million primarily for provisions for our promotional activity, as well as an increase in warranty liability consistent with the increase in revenue. The net increase in operating assets and liabilities was partially offset by a decrease of \$65.9 million in accounts payable and accrued expenses primarily due to the decrease in inventory, an increase of \$7.3 million in accounts receivable, net, and a decrease of \$4.0 million in deferred revenue.

Cash flows from investing activities

Cash used in investing activities for the three months ended December 31, 2022, of \$14.7 million was for the purchases of property and equipment, and intangible assets, which were primarily related to marketing-related product displays.

Cash flows from financing activities

Cash used in financing activities for the three months ended December 31, 2022, of \$15.3 million consisted primarily of payments for repurchases of common stock of \$15.0 million, payments for repurchases of common stock related to shares withheld for tax in connection with vesting of stock awards of \$8.4 million, offset by proceeds from the exercise of stock options of \$8.1 million.

Commitments and Contingencies

See Note 7. *Commitments and Contingencies* in the notes to condensed consolidated financial statements.

Off-Balance Sheet Arrangements

We have not entered into any off-balance sheet arrangements, except as described above, and do not have any holdings in variable interest entities.

Critical Accounting Policies and Estimates

Our unaudited condensed consolidated financial statements are prepared in accordance with U.S. GAAP. The preparation of these unaudited condensed consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses, and related disclosures. We evaluate our estimates and assumptions on an ongoing basis. Our estimates are based on historical experience and various other assumptions that we believe to be reasonable under the circumstances. Actual results could differ materially from those estimates.

Other than items discussed in Note 2 of our condensed consolidated financial statements, there have been no material changes to our critical accounting policies as compared to the critical accounting policies and significant judgments and estimates disclosed in our Annual Report on Form 10-K.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

We are exposed to financial market risks, including changes in currency exchange rates and interest rates. For quantitative and qualitative disclosures about market risk, refer to Part II, Item 7A, Quantitative and Qualitative Disclosures About Market Risk, in our Annual Report on Form 10-K. Our exposure to market risk has not changed materially, except as follows:

Foreign Currency Risk

Our inventory purchases are primarily denominated in U.S. dollars. Our international sales are primarily denominated in foreign currencies and any movement in the exchange rate between the U.S. dollar and the currencies in which we conduct sales in foreign countries could have an impact on our revenue, principally for sales

denominated in the euro and the British pound. A portion of our operating expenses are incurred outside the United States and are denominated in foreign currencies, which are also subject to foreign currency exchange rate fluctuations. In certain countries where we may invoice customers in the local currency our revenues benefit from a weaker dollar and are adversely affected by a stronger dollar. The opposite impact occurs in countries where we record expenses in local currencies. In those cases, our costs and expenses benefit from a stronger dollar and are adversely affected by a weaker dollar.

We do not currently use foreign exchange contracts or derivatives to hedge any foreign currency exposures. The volatility of exchange rates depends on many factors that we cannot forecast with reliable accuracy. Our continued international expansion increases our exposure to exchange rate fluctuations and, as a result, such fluctuations could have a significant impact on our future results of operations.

For the three months ended December 31, 2022, and January 1, 2022, we recognized a gain from foreign currency exchange of \$23.6 million and a loss from foreign currency exchange of \$1.4 million, respectively. Based on transactions denominated in currencies other than U.S. dollar as of December 31, 2022, a hypothetical adverse change of 10% would have resulted in an adverse impact on income before provision for income taxes of approximately \$11.1 million for the three months ended December 31, 2022.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including the Chief Executive Officer and Chief Financial Officer, we have evaluated the effectiveness of our disclosure controls and procedures as required under Rule 13a-15(b) under the Securities Exchange Act of 1934, as amended (“Exchange Act”) as of December 31, 2022. Based on that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that these disclosure controls and procedures were effective at a reasonable assurance level as of the end of the period covered by this Quarterly Report on Form 10-Q.

Changes in Internal Control

There were no changes in our internal control over financial reporting in management's evaluation pursuant to Rule 13a-15(f) during the quarter ended December 31, 2022, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

From time to time, we may become involved in legal proceedings or be subject to claims arising in the ordinary course of our business. Other than the matters described in Note 7 of the notes to our condensed consolidated financial statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q, we were not a party to any legal proceedings that in the opinion of our management, if determined adversely to us, would individually or taken together have a material adverse effect on our business, operating results, financial condition, or cash flows. Regardless of the outcome, litigation can have an adverse impact on us because of defense and settlement costs, diversion of management resources, and other factors.

Item 1A. Risk Factors

Investing in our common stock involves a high degree of risk. You should carefully consider the risks and uncertainties described below, as well as the other information in this Quarterly Report on Form 10-Q, including our condensed consolidated financial statements and the related notes, and the section titled "Management's Discussion and Analysis of Financial Condition and Results of Operations," before making an investment decision. The occurrence of any of the events or developments described below could materially and adversely affect our business, financial condition, results of operations, and growth prospects. In such an event, the market price of our common stock could decline, and you may lose all or part of your investment. Additional risks and uncertainties not currently known to us or that we currently believe are not material may also impair our business, financial condition, results of operations, and growth prospects.

Economic, Industry and Strategic Risk

Our business has been, and could in the future be, adversely affected by the ongoing COVID-19 pandemic.

The COVID-19 pandemic and related mitigation measures have adversely affected our business and operating results and may continue to impact us in the future. During the pandemic, consistent with its effects industry-wide, our supply chain experienced disruptions, including lockdowns, port congestion, component supply-related challenges, and inflationary pressures, which may continue in the future. Previous supply chain challenges increased our component and shipping and logistics costs, caused delayed product availability, and impacted our ability to forecast and meet product demand, procure certain components, and effectively manage our inventory levels, all of which has and could in the future, materially and adversely affected our business, results of operations, financial position, and cash flows. Although some pandemic-related impacts on our business have abated, they may emerge or intensify again given the uncertain course of the pandemic and its effects.

COVID-19 has also negatively impacted the global economy to date, including by contributing to significant global economic uncertainty. The duration and severity of the economic impacts of COVID-19 are unknown and may be prolonged and extend beyond the easing of mitigation measures, the widespread availability of vaccines and treatments or any eventual containment of the spread of COVID-19. In particular, any recession, depression, inflationary pressures, or other sustained adverse market event resulting from, among other causes, COVID-19 may result in high levels of unemployment and associated loss of personal income, decreased consumer confidence, and lower discretionary spending, which could materially and adversely affect our business, results of operations, financial position, and cash flows.

The extent of the impact of the COVID-19 pandemic on our business and operating results is uncertain and difficult to predict and will depend on factors outside of our control, including efforts to contain the spread of COVID-19, any resurgence of infections or any variants that may emerge and the impact of the pandemic on the global economy. Moreover, we have experienced increased demand for our products during much of the COVID-19 pandemic and we cannot predict how or whether the easing of COVID-19 mitigation measures will impact demand for our products or shift consumer spending habits in general. In the last half of fiscal 2022, we saw a softening of consumer demand in part as a result of a shift in consumer spending from purchasing goods to purchasing services and it is uncertain whether such shift will continue.

The home audio and consumer electronics industries are highly competitive.

The markets in which we operate are extremely competitive and rapidly evolving, and we expect that competition will intensify in the future. Our competition includes established, well-known sellers of speakers and sound systems such as Bose, Samsung (and its subsidiaries Harman International and JBL), Sony, Bang & Olufsen, and Masimo (and its subsidiary Sound United that owns, among others, the Denon, Polk Audio and Bowers and Wilkens brands), and developers of voice-enabled speakers and systems such as Amazon, Apple and Google. We could also face competition from new market entrants, some of whom might be current partners of ours.

In order to deliver products that appeal to changing and increasingly diverse consumer preferences and to overcome the fact that a relatively high percentage of consumers may already own or use products that they perceive to be similar to those that we offer, we must develop superior technology, anticipate increasingly diverse consumer tastes and rapidly develop attractive products with competitive selling prices. In addition, many of our current and potential partners have business objectives that may drive them to sell their speaker products at a significant discount compared to ours. Amazon and Google, for example, both currently offer their speaker products at significantly lower prices than our speaker products. Many of these partners may subsidize these prices and seek to monetize their customers through the sale of additional services rather than the speakers themselves. Even if we are able to efficiently develop and offer innovative products at competitive selling prices, our operating results and financial condition may be adversely impacted if we are unable to effectively anticipate and counter the ongoing price erosion that frequently affects consumer products or if the average selling prices of our products decrease faster than we are able to reduce our manufacturing costs.

Many of our competitors have greater financial, technical and marketing resources available to them than those available to us, and, as a result, they may develop competing products that cause the demand for our products to decline. Our competitors have established, or may establish, cooperative relationships among themselves or with third parties to increase the abilities of their products to address the needs of our prospective customers, and other companies may enter our markets by entering into strategic relationships with our competitors. A failure to effectively anticipate and respond to these established and new competitors may adversely impact our business and operating results.

Further, our current and prospective competitors may consolidate with each other or acquire companies that will allow them to develop products that better compete with our products, which would intensify the competition that we face and may also disrupt or lead to termination of our distribution, technology and content partnerships. For example, if one of our competitors were to acquire one of our content partners, the consolidated company may decide to disable the streaming functionality of its service with our products.

If we are unable to compete with these consolidated companies or if consolidation in the market disrupts our partnerships or reduces the number of companies we partner with, our business would be adversely affected.

To remain competitive and stimulate consumer demand, we must successfully manage frequent new product introductions and transitions.

Due to the quickly evolving and highly competitive nature of the home audio and broader consumer electronics industry, we must frequently introduce new products, enhance existing products and effectively stimulate customer demand for new and upgraded products in both mature and developing markets. For example, in June 2022 we introduced Ray, our compact soundbar and in September 2022 we introduced Sub Mini, the smaller of our two wireless subwoofer offerings. The successful introduction of these products and any new products depends on a number of factors, such as the timely completion of development efforts to correspond with limited windows for market introduction. We face significant challenges in managing the risks associated with new product introductions and production ramp-up issues, including accurately forecasting initial consumer demand, effectively managing any third-party strategic alliances or collaborative partnerships related to new product development or commercialization, as well as the risk that new products may have quality or other defects in the early stages of introduction or may not achieve the market acceptance necessary to generate sufficient revenue. New and upgraded products can also affect the sales and profitability of existing products. Accordingly, if we cannot properly manage the introduction of new products, our operating results and financial condition may be adversely impacted, particularly if the cadence of new product introductions increases as we expect.

Although we have achieved profitability, our business is impacted by a number of factors, including those outside of our control like the global economy, and we may not be able to sustain or increase our profitability and expect to incur increased operating costs in the future.

Although we achieved profitability starting in the fiscal year ended October 2, 2021, we may not be able to maintain or grow our profitability. We have experienced net losses in the past and may incur net losses in the future. We had an accumulated deficit of \$2.5 million as of October 1, 2022.

We expect our operating expenses to increase in the future as we expand our operations and execute on our product roadmap and strategy. We plan to make significant future expenditures related to the expansion of our business and our product offerings, including investments in:

- research and development to continue to introduce innovative new products, enhance existing products and improve our customers' listening experience;
- sales and marketing to expand our global brand awareness, promote new products, increase our customer base and expand sales within our existing customer base; and
- legal, accounting, information technology and other administrative expenses to sustain our operations as a public company.

In order to maintain or grow our profitability, we need to continue to increase our revenue and we cannot assure you that we will be able to do so, particularly during times of global economic, social and political uncertainty. For example, demand for our products was impacted in the last half of fiscal 2022, and in the future may be impacted, by uncertainty in the economic environment including the potential for an extended global recession, continued inflationary pressures, or, in certain markets, foreign currency exchange rate fluctuations, including those resulting from the Russian invasion of Ukraine. Our ability to achieve revenue growth will depend in part on our ability to execute on our product roadmap and our strategy and to determine the market opportunity for new products. New product introductions may adversely impact our gross margin in the near to intermediate term due to the frequency of these product introductions and their anticipated increased share of our overall product volume. The expansion of our business and product offerings also places a continuous and significant strain on our management, operational and financial resources. In the event that we are unable to grow our revenue, or in the event that revenue grows more slowly than we expect, our operating results could be adversely affected, and our stock price could be harmed.

Our investments in research and development may not yield the results expected.

Our business operates in intensely competitive markets characterized by changing consumer preferences and rapid technological innovation. Due to advanced technological innovation and the relative ease of technology imitation, new products tend to become standardized more rapidly, leading to more intense competition and ongoing price erosion. In order to strengthen the competitiveness of our products in this environment, we continue to invest heavily in research and development. However, these investments may not yield the innovation or the results expected on a timely basis, or our competitors may surpass us in technological innovation, hindering our ability to timely commercialize new and competitive products that meet the needs and demands of the market, which consequently may adversely impact our operating results as well as our reputation.

If we are not successful in continuing to expand our direct-to-consumer sales channel by driving consumer traffic and consumer purchases through our website, our business and results of operations could be harmed.

We have invested significant resources in our direct-to-consumer sales channel, primarily through our website, and our future growth relies, in part, on our continued ability to attract consumers to this channel, which has and will continue to require significant expenditures in marketing, software development and infrastructure. If we are unable to continue to drive traffic to, and increase sales through, our website, our business and results of operations could be harmed. The continued success of direct-to-consumer sales through our website is subject to risks associated with e-commerce, many of which are outside of our control. Our inability to adequately respond to these risks and uncertainties or to successfully maintain and expand our direct-to-consumer business via our website may have an adverse impact on our results of operations.

If we are unable to accurately anticipate market demand for our products, we may have difficulty managing our production and inventory and our operating results could be harmed.

We must forecast production and inventory needs in advance with our suppliers and manufacturers; our ability to do so accurately could be affected by many factors, including changes in customer demand and spending patterns, new product introductions, sales promotions, channel inventory levels, uncertainties related to the COVID-19 pandemic, Russia's invasion of Ukraine, and general economic conditions, including inflation and the potential for an extended global recession. If demand does not meet our forecast, excess product inventory could force us to write-down or write-off inventory or to sell the excess inventory at discounted prices, which could cause our gross margin to suffer and impair the strength of our brand. In addition, excess inventory may result in reduced working capital, which could adversely affect our ability to invest in other important areas of our business such as marketing and product development. If our channel partners have excess inventory of our products, they may decrease their purchases of our products in subsequent periods. If demand exceeds our forecast, as it did in parts of fiscal 2022, and we do not have sufficient inventory to meet this demand, we may experience decreased revenue or customer dissatisfaction as a result of any continued inventory shortages or we may have to rapidly increase production which may result in reduced manufacturing quality and customer satisfaction as well as higher supply and manufacturing costs that would lower our gross margin. Any of these scenarios could adversely impact our operating results and financial condition.

Our efforts to expand beyond our core product offerings and offer products with wider applications may not succeed and could adversely impact our business.

We may seek to expand beyond our core sound systems and develop products that have wider applications outside of home sound, such as commercial or office. Developing these products would require us to devote substantial additional resources, and our ability to succeed in developing such products to address such markets is unproven. It is likely that we would need to hire additional personnel, partner with new third parties and incur considerable research and development expenses to pursue such an expansion successfully. We may have less familiarity with consumer preferences for these products and less product or category knowledge, and we could encounter difficulties in attracting new customers due to lower levels of consumer familiarity with our brand. As a result, we may not be successful in future efforts to achieve profitability from new markets, services or new types of products, and our ability to generate revenue from our existing products may suffer. If any such expansion does not enhance our ability to maintain or grow our revenue or recover any associated development costs, our operating results could be adversely affected.

We experience seasonal demand for our products, and if our sales in high-demand periods are below our forecasts, our overall financial condition and operating results could be adversely affected.

Given the seasonal nature of our sales, accurate forecasting is critical to our business. Our fiscal year ends on the Saturday closest to September 30, the holiday shopping season occurs in the first quarter of our fiscal year and the typically slower summer months occur in the fourth quarter of our fiscal year. Historically, our revenue has been significantly higher in our first fiscal quarter due to increased consumer spending patterns during the holiday season. Any shortfalls in expected first fiscal quarter revenue, due to macroeconomic conditions like the potential for an extended global recession, product release patterns, a decline in the effectiveness of our promotional activities, supply chain disruptions, inflationary pressures or for any other reason, could cause our annual operating results to suffer significantly. In addition, if we fail to accurately forecast customer demand for the holiday season, we may experience excess inventory levels or a shortage of products available for sale, which could further harm our financial condition and operating results.

The success of our business depends in part on the continued growth of the voice-enabled speaker market and our ability to establish and maintain market share.

We have increasingly focused our product roadmap on voice-enabled speakers. We introduced our first voice-enabled speaker, Sonos One, in October 2017, our first voice-enabled home theater speaker, Sonos Beam, in July 2018, our first Bluetooth-enabled portable speaker with voice control, Sonos Move, in September 2019, and our voice-enabled premium home theater speaker, Sonos Arc, in June 2020. In April 2021, we introduced Roam, our portable smart speaker. In May 2022, we introduced Sonos Voice Control, our proprietary voice assistant, on our voice-enabled speakers. If the voice-enabled speaker markets do not continue to grow or grow in unpredictable ways, our revenue may fall short of expectations and our operating results may be harmed, particularly since we

incur substantial costs to introduce new products in advance of anticipated sales. Additionally, even if the market for voice-enabled speakers does continue to grow, we may not be successful in developing and selling speakers that appeal to consumers or gain sufficient market acceptance. To succeed in this market, we will need to design, produce and sell innovative and compelling products and partner with other businesses that enable us to capitalize on new technologies, some of which have developed or may develop and sell voice-enabled speaker products of their own as further described herein.

If market demand for streaming music does not grow as anticipated or the availability and quality of streaming services does not continue to increase, our business could be adversely affected.

A large proportion of our customer base uses our products to listen to content via subscription-based streaming music services. Accordingly, we believe our future revenue growth will depend in significant part on the continued expansion of the market for streaming music. The success of the streaming music market depends on the quality, reliability and adoption of streaming technology and on the continued success of streaming music services such as Apple Music, Spotify, Deezer, and Pandora. If the streaming music market in general fails to expand or if the streaming services that we partner with are not successful, demand for our products may suffer and our operating results may be adversely affected.

If we are unable to protect our intellectual property, the value of our brand and other intangible assets may be diminished, and our business may be adversely affected.

We rely and expect to continue to rely on a combination of confidentiality and license agreements with our employees, consultants and third parties with whom we have relationships, as well as patent, trademark, copyright and trade secret protection laws, to protect our proprietary rights. In the United States and certain other countries, we have filed various applications for certain aspects of our intellectual property, most notably patents. However, third parties may knowingly or unknowingly infringe our proprietary rights or challenge our proprietary rights, pending and future patent and trademark applications may not be approved, and we may not be able to prevent infringement without incurring substantial expense. Such infringement could have a material adverse effect on our brand, business, financial condition and results of operations. We have initiated legal proceedings to protect our intellectual property rights, and we may file additional actions in the future. For example, in January 2020 we filed a complaint with the ITC against Alphabet and Google and a counterpart lawsuit in the U.S. District Court for the Central District of California against Google alleging infringement of five Sonos patents, and in September 2020 we filed another lawsuit against Google alleging infringement of an additional four Sonos patents. The cost of defending our intellectual property has been and may in the future be substantial, and there is no assurance we will be successful. Our business could be adversely affected as a result of any such actions, or a finding that any patents-in-suit are invalid or unenforceable. These actions have led and may in the future lead to additional counterclaims or actions against us, which are expensive to defend against and for which there can be no assurance of a favorable outcome. For example, Google has responded to our legal proceedings by filing multiple patent infringement lawsuits against us in the U.S. District Court for the Northern District of California, cases against us in the ITC, and patent infringement lawsuits against us and our subsidiary Sonos Europe B.V. in various foreign jurisdictions. Further, parties we bring legal action against could retaliate through non-litigious means, which could harm our ability to compete against such parties or to enter new markets.

In addition, the regulations of certain foreign countries do not protect our intellectual property rights to the same extent as the laws of the United States. As our brand grows, we may discover unauthorized products in the marketplace that are counterfeit reproductions of our products. If we are unsuccessful in pursuing producers or sellers of counterfeit products, continued sales of these products could adversely impact our brand, business, financial condition and results of operations.

We currently are, and may continue to be, subject to intellectual property rights claims and other litigation which are expensive to support, and if resolved adversely, could have a significant impact on us and our stockholders.

Companies in the consumer electronics industries own large numbers of patents, copyrights, trademarks, domain names and trade secrets, and frequently enter into litigation based on allegations of infringement, misappropriation or other violations of intellectual property or other rights. As we gain an increasingly high profile and face more intense competition in our markets, and as we introduce more products and services, including through acquisitions and through partners, the possibility of intellectual property rights claims against us grows.

Our technologies may not be able to withstand any third-party claims or rights against their use, and we may be subject to litigation and disputes. The costs of supporting such litigation and disputes are considerable, and there can be no assurance that a favorable outcome would be obtained. We may be required to settle such litigation and disputes, or we may be subject to an unfavorable judgment in a trial, and the terms of a settlement or judgment against us may be unfavorable and require us to cease some or all our operations, limit our ability to use certain technologies, pay substantial amounts to the other party or issue additional shares of our capital stock to the other party, which would dilute our existing stockholders. Further, if we are found to have engaged in practices that are in violation of a third party's rights, we may have to negotiate a license to continue such practices, which may not be available on reasonable or favorable terms, or may have to develop alternative, non-infringing technology or discontinue the practices altogether. In the event that these practices relate to an acquisition or a partner, we may not be successful in exercising any indemnification rights available to us under our agreements or in recovering damages in the event that we are successful. Each of these efforts could require significant effort and expense and ultimately may not be successful.

If we are not able to maintain and enhance the value and reputation of our brand, or if our reputation is otherwise harmed, our business and operating results could be adversely affected.

Our continued success depends on our reputation for providing high-quality products and consumer experiences, and the "Sonos" name is critical to preserving and expanding our business. Our brand and reputation are dependent on a number of factors, including our marketing efforts, product quality, and trademark protection efforts, each of which requires significant expenditures.

The value of our brand could also be severely damaged by isolated incidents, which may be outside of our control. For example, in the United States, we rely on custom installers of home audio systems for a significant portion of our sales but maintain no control over the quality of their work and thus could suffer damage to our brand or business to the extent such installations are unsatisfactory or defective. Any damage to our brand or reputation may adversely affect our business, financial condition and operating results.

Conflicts with our channel and distribution partners could harm our business and operating results.

Several of our existing products compete, and products that we may offer in the future could compete, with the product offerings of some of our significant channel and distribution partners who have greater financial and technical resources than we do. To the extent products offered by our partners compete with our products, they may choose to market and promote their own products over ours or could end our partnerships and cease selling or promoting our products entirely. Any reduction in our ability to place and promote our products, or increased competition for available shelf or website placement, especially during peak retail periods, such as the holiday shopping season, would require us to increase our marketing expenditures and to seek other distribution channels to promote our products. If we are unable to effectively sell our products due to conflicts with our distribution partners or the inability to find alternative distribution channels, our business would be harmed.

The expansion of our direct-to-consumer channel could alienate some of our channel partners and cause a reduction in product sales from these partners. Channel partners may perceive themselves to be at a disadvantage based on the direct-to-consumer sales offered through our website. Due to these and other factors, conflicts in our sales channels could arise and cause channel partners to divert resources away from the promotion and sale of our products. Further, to the extent we use our mobile app to increase traffic to our website and increase direct-to-consumer sales, we will rely on application marketplaces such as the Apple App Store and Google Play to drive downloads of our mobile app. Apple and Google, both of which sell products that compete with ours, may choose to use their marketplaces to promote their competing products over our products or may make access to our mobile app more difficult. Any of these situations could adversely impact our business and results of operations.

Competition with our technology partners could harm our business and operating results.

We are dependent on a number of technology partners for the development of our products, some of which have developed or may develop and sell products that compete with our products. These technology partners may cease doing business with us or disable the technology they provide our products for a variety of reasons, including to promote their products over our own. For example, we are currently manufacturing and developing voice-enabled speaker systems that are enhanced with the technology of our partners, including those who sell competing products. We introduced Sonos One, Sonos Beam, Sonos Move, Sonos Roam, and Sonos Arc, which feature built-in

voice-enabled speakers powered by Amazon's Alexa or Google's Google Assistant technology. One or more of our partners could disable their integration on one or all of our voice-enabled products, terminate or not renew their distribution agreement with us, or begin charging us for their integration with our voice-enabled products. For example, our current agreement with Amazon allows Amazon to disable the Alexa integration in our voice-enabled products with limited notice. We cannot assure you that we will be successful in establishing partnerships with other companies that have developed voice-control enablement technology or in developing such technology on our own.

If one or more of our technology partners do not maintain their integration with our products or seek to charge us for this integration, or if we have not developed alternative partnerships for similar technology or developed such technology on our own, our sales may decline, our reputation may be harmed and our business and operating results may suffer.

Competition with our content partners could cause these partners to cease to allow their content to be streamed on our products, which could lower product demand.

Demand for our products depends in large part on the availability of streaming third-party content that appeals to our existing and prospective customers. Compatibility with streaming music services, podcast platforms and other content provided by our content partners is a key feature of our products. To date, all our arrangements have been entered into on a royalty-free basis. Some of these content partners compete with us already, and others may in the future produce and sell speakers along with their streaming services. Additionally, other content partners may form stronger alliances with our competitors in the home audio market. Any of our content partners may cease to allow their content to be streamed on our products for a variety of reasons, including as a result of our offering competing services, to promote other partnerships or their products over our products, or to seek to charge us for this streaming. If this were to happen, demand for our products could decrease, our costs could increase and our operating results could be harmed.

Operational Risks

We are dependent on a limited number of contract manufacturers to manufacture our products and our efforts to diversify manufacturers may not be successful.

We depend on a limited number of contract manufacturers to manufacture our products, with our key manufacturer, Inventec Appliances Corporation, manufacturing a majority of our products. We have also historically manufactured our products in China. In fiscal 2020, we began our efforts to diversify our supply chain through the addition of new contract manufacturers and geographic diversification, starting with Malaysia and extending such efforts into Vietnam in fiscal 2022. Our reliance on a limited number of contract manufacturers increases the risk that, in the event that any or all of such manufacturers experience an interruption in their operations, fail to perform their obligation in a timely manner or terminate agreements with us, we would not be able to maintain our production capacity without incurring material additional costs and substantial delays or we may be fully prevented from selling our products. Any material disruption in our relationship with our manufacturers would harm our ability to compete effectively and satisfy demand for our products and could adversely impact our revenue, gross margin and operating results.

In addition, there is no guarantee that our efforts to diversify manufacturers will be successful. Identifying and onboarding a new manufacturer takes a significant amount of time and resources. If we do not successfully coordinate the timely manufacturing and distribution of our products by such manufacturers, if such manufacturers are unable to successfully and timely process our orders or if we do not receive timely and accurate information from such manufacturers, we may have an insufficient supply of products to meet customer demand, we may lose sales, we may experience a build-up in inventory, we may incur additional costs, and our financial performance and reporting may be adversely affected. By adding manufacturers in other countries, we may experience increased transportation costs, fuel costs, labor unrest, impact of natural disasters and other adverse effects on our ability, timing and cost of delivering products, which may increase our inventory, decrease our margins, adversely affect our relationships with distributors and other customers and otherwise adversely affect our operating results and financial condition. In addition, any partial or full government-mandated shutdown resulting from COVID-19 may impact or delay our efforts to diversify our supply chain or may cause supply chain disruptions notwithstanding any supply chain diversification efforts.

We depend on a limited number of third-party components suppliers and logistics providers, and many of our components have long lead times, and our business and operating results could be adversely affected by shortages, disruptions and related challenges.

We are dependent on a limited number of suppliers for various key components used in our products, and we may from time to time have sole source suppliers. The cost, quality and availability of these components are essential to the successful production and sale of our products. We are subject to the risk of industry-wide shortages, price fluctuations and long lead times in the supply of these components and other materials, which risk has been and may continue to be heightened by the impact of COVID-19. If the supply of these components is delayed or constrained, or if one or more of our main suppliers were to go out of business, alternative sources or suppliers may not be available on acceptable terms or at all. In the event that any of our suppliers were to discontinue production of our key product components, developing alternate sources of supply for these components would be time consuming, difficult and costly. In the event we are unable to obtain components in sufficient quantities on a timely basis and on commercially reasonable terms, our ability to sell our products in order to meet market demand would be affected and could materially and adversely affect our brand, image, business prospects and operating results.

In addition, the longer lead time for many of our components presents challenges in our efforts to manage component inventory, as we procure such components based on our then current forecast of demand for our products. During the pandemic, we have also faced the challenge of managing component inventory during periods of fluctuating availability. In particular, many components with longer lead times have experienced shortages during the pandemic and, as a result, during fiscal 2022 and the first quarter of fiscal 2023 we increased our investments in, and purchase commitments for, certain components where possible to secure inventory in anticipation of shortages and strong demand, and we may need to do so again in the future. In the event that actual demand for our products differs from our forecast, we may end up with an excess inventory of components, as we saw in the fourth quarter of fiscal 2022 and the first quarter of fiscal 2023, negatively impacting our working capital.

We also use a small number of logistics providers for substantially all our product delivery to both distributors and retailers. If one of these providers were to experience financial difficulties or disruptions in its business, or be subject to closures or other disruptions as a result of COVID-19, our own operations could be adversely affected. Because substantially all of our products are distributed from and into a small number of locations and by a small number of companies, we are susceptible to both isolated and system-wide interruptions caused by events out of our control, including COVID-19 lockdowns. Any disruption to the operations of our distribution facilities could delay product delivery, harm our reputation among our customers and adversely affect our operating results and financial condition.

We have limited control over the third-party suppliers and logistics providers on which our business depends. If any of these parties fails to perform its obligations to us, we may be unable to deliver our products to customers in a timely manner. Further, we do not have long-term contracts with all of these parties, and there can be no assurance that we will be able to renew our contracts with them on favorable terms or at all. We may be unable to replace an existing supplier or logistics provider or supplement a provider in the event we experience significantly increased demand. Accordingly, a loss or interruption in the service of any key party could adversely impact our revenue, gross margin and operating results.

We sell our products through a limited number of key channel partners, and the loss of any such channel partner would adversely impact our business.

We are dependent on our channel partners for a vast majority of our product sales. Best Buy, one of our key channel partners, accounted for 15% of our revenue in fiscal 2022. We compete with other consumer products for placement and promotion of our products in the stores of our channel partners, including in some cases products of our channel partners. Our contracts with our channel partners allow them to exercise significant discretion in the placement and promotion of our products, and such contracts do not contain any long-term volume commitments. If one or several of our channel partners do not effectively market and sell our products, discontinue or reduce the inventory of our products, increase the promotions of or choose to promote competing products over ours, the volume of our products sold to customers could decrease, and our business and results of operations would therefore be significantly harmed. Many of our key channel partners temporarily closed or reduced operations in their retail

stores at various times during the pandemic and may continue to do so in the future, which has had, and may continue to have, a material effect on our business and results of operations.

Revenue from our channel partners also depends on a number of factors outside our control and may vary from period to period. One or more of our channel partners may experience serious financial difficulty, particularly in light of the impact of the pandemic on the retail sector, may consolidate with other channel partners or may have limited or ceased operations. Our business and results of operations have been, and may continue to be, significantly harmed by retail store closures by many of our key channel partners. Loss of a key channel partner would require us to identify alternative channel partners or increase our reliance on our direct-to-consumer channel, which may be time-consuming and expensive or we may be unsuccessful in our efforts to do so.

We have and may in the future discontinue support for older versions of our products, resulting in customer dissatisfaction that could negatively affect our business and operating results.

We have historically maintained, and we believe our customers may expect, extensive backward compatibility for our older products and the software that supports them, allowing older products to continue to benefit from new software updates. We expect that as we continue to improve and enhance our software platform, this backward compatibility will no longer be practical or cost-effective, and we may decrease or discontinue service for our older products. For example, certain of our legacy products continue to work but no longer receive software updates (other than bug fixes and patches). To the extent we no longer provide extensive backward capability for our products, we may damage our relationship with our existing customers, as well as our reputation, brand loyalty and ability to attract new customers.

For these reasons, any decision to decrease or discontinue backward capability may decrease sales, generate legal claims and adversely affect our business, operating results and financial condition.

Product quality issues and a higher-than-expected number of warranty claims or returns could harm our business and operating results.

The products that we sell could contain defects in design or manufacture. Defects could also occur in the products or components that are supplied to us. There can be no assurance we will be able to detect and remedy all defects in the hardware and software we sell, which could result in product recalls, product redesign efforts, loss of revenue, reputational damage and significant warranty and other remediation expenses. Similar to other consumer electronics, our products have a risk of overheating and fire in the course of usage or upon malfunction. Any such defect could result in harm to property or in personal injury. If we determine that a product does not meet product quality standards or may contain a defect, the launch of such product could be delayed until we remedy the quality issue or defect. The costs associated with any protracted delay necessary to remedy a quality issue or defect in a new product could be substantial.

We generally provide a one-year warranty on all our products, except in the European Union ("EU") and select other countries where we provide a minimum two-year warranty, depending on the region, on all our products. The occurrence of any material defects in our products could expose us to liability for warranty claims in excess of our current reserves, and we could incur significant costs to correct any defects, warranty claims or other problems. In addition, our failure to comply with past, present and future laws regulating extended warranties and accidental damage coverage could result in reduced sales of our products, reputational damage, penalties and other sanctions, which could harm our business and financial condition.

Our international operations are subject to increased business and economic risks that could impact our financial results.

We have operations outside the United States, and we expect to continue to expand our international presence, especially in Asia. In fiscal 2022, 45% of our revenue was generated outside the United States. This subjects us to a variety of risks inherent in doing business internationally, including:

- fluctuations in currency exchange rates and costs of imposing currency exchange controls;
- political, social and/or economic instability, including related to the ongoing COVID-19 pandemic, Russia's invasion of Ukraine and the United Kingdom's withdrawal from the EU, commonly known as "Brexit";

- tariffs, trade barriers and duties;
- protectionist laws and business practices that favor local businesses in some countries;
- higher levels of credit risk and payment fraud and longer payment cycles associated with, and increased difficulty of payment collections from certain international customers;
- burdens and risks of complying with a number and variety of foreign laws and regulations, including the Foreign Corrupt Practices Act;
- laws and regulations may change from time to time unexpectedly and may be unpredictably enforced;
- potential negative consequences from changes in or interpretations of U.S. and foreign tax laws;
- the cost of developing connected products for countries where Wi-Fi technology has been passed over in favor of more advanced cellular data networks;
- reduced protection for intellectual property rights in some countries;
- difficulties and associated costs in managing and staffing multiple international locations; and
- delays from customs brokers or government agencies.

If we are unable to manage the complexity of our global operations successfully, or if the risks above become substantial for us, our financial performance and operating results could suffer. Further, any measures that we may implement to reduce risks of our international operations may not be effective, may increase our expenses and may require significant management time and effort. Entry into new international markets requires considerable management time and financial resources related to market, personnel and facilities development before any significant revenue is generated. As a result, initial operations in a new market may operate at low margins or may be unprofitable.

We have significant operations in China, where many of the risks listed above are particularly acute. China experiences high turnover of direct labor due to the intensely competitive and fluid market for labor, and if our labor turnover rates are higher than we expect in that region, or we otherwise fail to adequately manage our labor needs, then our business and results of operations could be adversely affected.

We will need to improve our financial and operational systems to manage our growth effectively and support our increasingly complex business arrangements, and an inability to do so could harm our business and results of operations.

To manage our growth and our increasingly complex business operations, especially as we move into new markets internationally, we will need to upgrade our operational and financial systems and procedures, which requires management time and may result in significant additional expense. In particular, we replaced our legacy ERP system in order to accommodate our expanding operations. We cannot be certain that we will institute, in a timely or efficient manner or at all, the improvements to our managerial, operational and financial systems and procedures necessary to support our anticipated increased levels of operations. Problems associated with, or disruptions resulting from, any improvement or expansion of our operational and financial systems could adversely affect our relationships with our suppliers, manufacturers, resellers and customers, inhibit our ability to expand or take advantage of market opportunities, cause harm to our reputation, result in errors in our financial and other reporting, and affect our ability to maintain an effective internal control environment and meet our external reporting obligations, any of which could harm our business and operating results and affect our stock price.

A significant disruption in our websites, servers or information technology systems, or those of our third-party partners, could impair our customers' listening experience or otherwise adversely affect our customers, damage our reputation or harm our business.

As a consumer electronics company, our website and mobile app are important presentations of our business, identity and brand and an important means of interacting with, and providing information to, consumers of our products. We depend on our servers and centralized information technology systems, and those of third parties, for product functionality, to manage operations and to store critical information and intellectual property. Accordingly, we allocate significant resources to maintaining our information technology systems and deploying network security, data encryption, training and other measures to protect against unauthorized access or misuse.

Nevertheless, our website and information technology systems, and those of the third parties we rely on, are susceptible to damage, viruses, disruptions or shutdowns due to foreseeable and unforeseeable events. System failures and disruptions could impede the manufacturing and shipping of products, functionality of our products, transactions processing and financial reporting, and result in the loss of intellectual property or data, require substantial repair costs and damage our reputation, competitive position, financial condition and results of operations.

For example, we use Amazon Web Services ("AWS") to maintain the interconnectivity of our mobile app to our servers and those of the streaming services that our customers access to enjoy our products. Because AWS runs its own platform that we access, we are vulnerable to both system-wide and Sonos-specific service outages at AWS. Our access to AWS' infrastructure could be limited by a number of potential causes, including technical failures, natural disasters, fraud or security attacks that we cannot predict or prevent.

Additionally, our products may contain flaws that make them susceptible to unauthorized access or use. For example, we previously discovered a vulnerability in our products that could be exploited when a customer visited a website with malicious content, allowing the customer's local network to be accessed by third parties who could then gain unauthorized access to the customer's playlists and other data and limited control of the customer's devices. While we devote significant resources to address and eliminate flaws and other vulnerabilities in our products, there can be no assurance that our products will not be compromised in the future. Any such flaws or vulnerabilities, whether actual or merely potential, could harm our reputation, competitive position, financial condition and results of operations.

Any cybersecurity breaches or our actual or perceived failure to comply with such legal obligations by us, or by our third-party service providers or partners, could harm our business.

We collect, store, process and use our customers' personally identifiable information and other data, and we rely on third parties that are not directly under our control to do so as well. While we take measures intended to protect the security, integrity and confidentiality of the personal information and other sensitive information we collect, store or transmit, we cannot guarantee that inadvertent or unauthorized use or disclosure will not occur, or that third parties will not gain unauthorized access to this information. There have been a number of recent reported incidents where third parties have used software to access the personal data of their partners' customers for marketing and other purposes.

If we or our third-party service providers were to experience a breach, disruption or failure of systems compromising our customers' data, or if one of our third-party service providers or partners were to access our customers' personal data without our authorization, our brand and reputation could be adversely affected, use of our products could decrease and we could be exposed to a risk of loss, litigation and regulatory proceedings. In addition, a breach could require expending significant additional resources related to the security of information systems and disrupt our operations.

The use of data by our business and our business associates is highly regulated in all our operating countries. Privacy and information security laws and regulations change, and compliance with them may result in cost increases due to, among other things, systems changes and the development of new processes. If we or those with whom we share information fail to comply with laws and regulations, such as the General Data Protection Regulation ("GDPR") and California Consumer Privacy Act ("CCPA"), our reputation could be damaged, possibly resulting in lost business, and we could be subjected to additional legal risk or financial losses as a result of non-compliance. Complying with such laws may also require us to modify our data processing practices and policies and incur substantial expenditures.

Changes in how network operators manage data that travels across their networks or in net neutrality rules could harm our business.

We rely upon the ability of consumers to access our service through the internet. If network operators block, restrict or otherwise impair access to our service over their networks, our service and business could be negatively affected. To the extent that network operators implement usage-based pricing, including meaningful bandwidth caps, or otherwise try to monetize access to their networks by data providers, we could incur greater operating

expenses. Furthermore, to the extent network operators create tiers of internet access service and either charge us for or prohibit us from being available through these tiers, our business could be negatively impacted.

Further, in the past, internet service providers ("ISPs") have attempted to implement usage-based pricing, bandwidth caps and traffic shaping or throttling. To the extent network operators create tiers of internet access service and charge our customers in direct relation to their consumption of audio content, our ability to attract and retain customers could be impaired, which would harm our business. Net neutrality rules, which were designed to ensure that all online content is treated the same by ISPs and other companies that provide broadband services, were repealed by the Federal Communications Commission ("FCC") effective June 2018. Although the FCC has preempted state jurisdiction over net neutrality, some states have taken executive action directed at reinstating aspects of the FCC's 2015 order. Further, while many countries, including across the EU, have implemented net neutrality rules, in others, the laws may be nascent or non-existent. The absence or repeal of the net neutrality rules could force us to incur greater operating expenses, cause our streaming partners to seek to shift costs to us or result in a decrease in the streaming-based usage of our platform by our customers, any of which would harm our results of operations. In addition, given uncertainty around these rules, including changing interpretations, amendments or repeal, coupled with potentially significant political and economic power of local network operators, we could experience discriminatory or anti-competitive practices that could impede our growth, cause us to incur additional expense or otherwise negatively affect our business.

Our use of open source software could negatively affect our ability to sell our products and subject us to possible litigation.

We incorporate open source software into our products, and we may continue to incorporate open source software into our products in the future. Open source software is generally licensed by its authors or other third parties under open source licenses. Some of these licenses contain requirements that we make available source code for modifications or derivative works we create based upon the open source software and that we license such modifications or derivative works under the terms of a particular open source license or other license granting third parties certain rights of further use. Additionally, if a third-party software provider has incorporated open source software into software that we license from such provider, we could be required to disclose any of our source code that incorporates or is a modification of our licensed software. If an author or other third party that distributes open source software that we use or license were to allege that we had not complied with the conditions of the applicable license, we could be required to incur significant legal expenses defending against those allegations and could be subject to significant damages, enjoined from offering or selling our products that contained the open source software and required to comply with the above conditions. Any of the foregoing could disrupt and harm our business and financial condition.

Legal and Regulatory Risks

Changes in international trade policies, including the imposition of tariffs have had, and may continue to have, an adverse effect on our business, financial condition and results of operations.

Under the previous administration, the U.S. government has imposed significant new tariffs on China related to the importation of certain product categories, including those under the August 2019 Section 301 Tariff Action (List 4A) ("Section 301 tariffs"). These Section 301 tariffs have increased our cost of revenue and adversely impacted our results of operations. We were able to obtain an exemption from the Section 301 tariffs for certain of our products for a period of time during fiscal 2020 and, for our core speaker products, through the first quarter of fiscal 2021. In March 2022, we obtained an additional exclusion exemption for our core speaker products for the period from October 12, 2021 to December 31, 2022. On December 16, 2022, the USTR granted an extension through September 30, 2023 of the exclusion for our core speaker products. To date, we have been able to obtain certain refunds on tariffs paid during the fiscal 2020, fiscal 2021, and fiscal 2022 exemption periods and continue to see outstanding refund requests and corresponding refunds processed for such periods.

In the event that future tariffs are imposed on imports of our products, we do not successfully obtain the remaining refunds to which we are currently entitled, we are not successful in any future exemption requests, the amounts of existing tariffs are increased, our efforts to diversify our supply chain outside of China are delayed or otherwise not successful, or China or other countries take retaliatory trade measures in response to existing or future tariffs, our business may be impacted and we may be required to raise prices or make changes to our operations, any of which could materially harm our revenue or operating results. In response to future new tariffs, we may

intensify our efforts to diversify outside of China, resulting in significant costs and disruption to our operations as we would need to pursue the time-consuming processes of recreating new supply chains, identifying substitute components and establishing new manufacturing locations.

We must comply with extensive regulatory requirements, and the cost of such compliance, and any failure to comply, may adversely affect our business, financial condition and results of operations.

In our current business and as we expand into new markets and product categories, we must comply with a wide variety of laws, regulations, standards and other requirements governing, among other things, electrical safety, wireless emissions, health and safety, e-commerce, consumer protection, export and import requirements, hazardous materials usage, product related energy consumption, packaging, recycling and environmental matters. Compliance with these laws, regulations, standards and other requirements may be onerous and expensive, and they may be inconsistent from jurisdiction to jurisdiction or change from time to time, further increasing the cost of compliance and doing business. Our products may require regulatory approvals or satisfaction of other regulatory concerns in the various jurisdictions in which they are manufactured, sold or both. These requirements create procurement and design challenges that require us to incur additional costs identifying suppliers and manufacturers who can obtain and produce compliant materials, parts and products. Failure to comply with such requirements can subject us to liability, additional costs and reputational harm and, in extreme cases, force us to recall products or prevent us from selling our products in certain jurisdictions.

We may incur costs in complying with changing tax laws in the United States and abroad, which could adversely impact our cash flow, financial condition and results of operations.

We are a U.S.-based company subject to taxes in multiple U.S. and foreign tax jurisdictions. Our profits, cash flow and effective tax rate could be adversely affected by changes in the tax rules and regulations in the jurisdictions in which we do business, unanticipated changes in statutory tax rates and changes to our global mix of earnings. As we expand our operations, any changes in the U.S. or foreign taxation of such operations may increase our worldwide effective tax rate.

We are also subject to examination by the Internal Revenue Service ("IRS") and other tax authorities, including state revenue agencies and foreign governments. If any tax authority disagrees with any position we have taken, our tax liabilities and operating results may be adversely affected. While we regularly assess the likelihood of favorable or unfavorable outcomes resulting from examinations by the IRS and other tax authorities to determine the adequacy of our provision for income taxes, there can be no assurance that the actual outcome resulting from these examinations will not materially adversely affect our financial condition and results of operations. In addition, the distribution of our products subjects us to numerous complex and often-changing customs regulations. Failure to comply with these systems and regulations could result in the assessment of additional taxes, duties, interest and penalties. There is no assurance that tax and customs authorities agree with our reporting positions and upon audit may assess us additional taxes, duties, interest and penalties. If this occurs and we cannot successfully defend our position, our profitability will be reduced.

Our ability to use our net operating loss carryforwards and certain other tax attributes may be limited.

As of October 1, 2022, we had gross U.S. federal net operating loss carryforwards of \$105.8 million, of which \$74.7 million have an indefinite life and \$31.1 million that expire beginning in 2035, and gross state net operating loss carryforwards of \$65.5 million, which expire beginning in 2027, as well as \$41.7 million in foreign net operating loss carryforwards with an indefinite life. As of October 1, 2022, we also had U.S. federal research and development tax credit carryforwards of \$70.0 million, and state research and development tax credit carryforwards of \$48.1 million, which will expire beginning in 2025 and 2024, respectively. Because of the change of ownership provisions of Sections 382 and 383 of the Code, use of a portion of the Company's domestic net operating losses and tax credit carryforwards may be limited in future periods depending upon future changes in ownership. Further, a portion of the carryforwards may expire before being applied to reduce future income tax liabilities if sufficient taxable income is not generated in future periods.

Risks Related to Ownership of Our Common Stock

The stock price of our common stock has been and may continue to be volatile or may decline regardless of our operating performance.

The stock price of our common stock has been and may continue to be volatile. The stock price of our common stock may fluctuate significantly in response to numerous factors in addition to the ones described in the preceding Risk Factors, many of which are beyond our control, including:

- overall performance of the equity markets and the economy as a whole;
- changes in the financial projections we or third parties may provide to the public or our failure to meet these projections;
- actual or anticipated changes in our growth rate relative to that of our competitors;
- announcements of new products, or of acquisitions, strategic partnerships, joint ventures or capital-raising activities or commitments, by us or by our competitors;
- additions or departures of key personnel;
- failure of securities analysts to maintain coverage of us, changes in financial estimates by any securities analysts who follow our company or our failure to meet these estimates or the expectations of investors;
- rumors and market speculation involving us or other companies in our industry;
- sales of shares of our common stock by us or our stockholders particularly sales by our directors, executive officers and significant stockholders, or the perception that these sales could occur; and
- additional stock issuances that result in significant dilution to shareholders.

In addition, the stock market with respect to companies in the technology industry has experienced significant price and volume fluctuations that have affected and continue to affect the stock prices of these companies. In the past, stockholders have instituted securities class action litigation following periods of market volatility. If we were to become involved in securities litigation, it could subject us to substantial costs, divert resources and the attention of management from our business and adversely affect our business.

We do not intend to pay dividends for the foreseeable future.

We have never declared or paid any cash dividends on our common stock, and we do not intend to pay any cash dividends in the foreseeable future. We anticipate that we will retain all our future earnings for use in the development of our business and for general corporate purposes. Any determination to pay dividends in the future will be at the discretion of the Board. Accordingly, investors must rely on sales of their common stock after price appreciation, which may never occur, as the only way to realize any future gains on their investments. In addition, the terms of our credit facilities contain restrictions on our ability to declare and pay cash dividends on our capital stock.

Certain provisions in our corporate charter documents and under Delaware law may prevent or hinder attempts by our stockholders to change our management or to acquire a controlling interest in us.

There are provisions in our restated certificate of incorporation and restated bylaws that may make it difficult for a third party to acquire, or attempt to acquire, control of our company, even if a change in control were considered favorable by our stockholders. These anti-takeover provisions include:

- a classified Board so that not all members of the Board are elected at one time;
- the ability of the Board to determine the number of directors and fill any vacancies and newly created directorships;
- a requirement that our directors may only be removed for cause;
- a prohibition on cumulative voting for directors;

- the requirement of a super-majority to amend some provisions in our restated certificate of incorporation and restated bylaws;
- authorization of the issuance of “blank check” preferred stock that the Board could use to implement a stockholder rights plan;
- an inability of our stockholders to call special meetings of stockholders; and
- a prohibition on stockholder actions by written consent, thereby requiring that all stockholder actions be taken at a meeting of our stockholders.

In addition, our restated certificate of incorporation provides that the Delaware Court of Chancery is the exclusive forum for any derivative action or proceeding brought on our behalf; any action asserting a breach of fiduciary duty; any action asserting a claim against us arising pursuant to the Delaware General Corporation Law (the “DGCL”), our restated certificate of incorporation or our restated bylaws; or any action asserting a claim against us that is governed by the internal affairs doctrine. Our restated certificate of incorporation also provides that the federal district courts of the United States will be the exclusive forum for resolving any complaint asserting a cause of action arising under the Securities Act of 1933, as amended.

Further, Section 203 of the DGCL may discourage, delay or prevent a change in control of our company. Section 203 imposes certain restrictions on mergers, business combinations, and other transactions between us and holders of 15% or more of our common stock.

General Risk Factors

The loss of one or more of our key personnel, or our failure to attract, assimilate and retain other highly qualified personnel in the future, could harm our business.

We depend on the continued services and performance of our key personnel. The loss of key personnel, including key members of management as well as our product development, marketing, sales and technology personnel, could disrupt our operations and have an adverse effect on our ability to grow our business. In addition, the loss of key personnel in our finance and accounting departments could harm our internal controls, financial reporting capability and capacity to forecast and plan for future growth. Further, the market for highly skilled workers and leaders in our industry is extremely competitive. If we do not succeed in attracting, hiring and integrating high-quality personnel or in retaining and motivating existing personnel, we may be unable to grow effectively, and our financial condition may be harmed.

Natural disasters, geopolitical unrest, war, terrorism, pandemics, public health issues or other catastrophic events could disrupt the supply, delivery or demand of products, which could negatively affect our operations and performance.

We are subject to the risk of disruption by earthquakes, floods and other natural disasters, fire, power shortages, geopolitical unrest, war, including Russia’s invasion of Ukraine, terrorist attacks and other hostile acts, public health issues, epidemics or pandemics, including COVID-19, and other events beyond our control and the control of the third parties on which we depend. Any of these catastrophic events, whether in the United States or abroad, may have a strong negative impact on the global economy, us, our contract manufacturers, our suppliers or customers, and could decrease demand for our products, create delays and inefficiencies in our supply chain and make it difficult or impossible for us to deliver products to our customers. Further, our headquarters are located in Santa Barbara, California, in a seismically active region that is also prone to forest fires. Any catastrophic event that occurred near our headquarters, or near our manufacturing facilities in China, Malaysia or Vietnam, could impose significant damage to our ability to conduct our business and could require substantial recovery time, which could have an adverse effect on our business, operating results and financial condition.

We may need additional capital, and we cannot be certain that additional financing will be available.

In October 2021, we entered into a credit agreement with JPMorgan Chase Bank, N.A., Bank of America N.A., Morgan Stanley Senior Funding, Inc., and Goldman Sachs Bank USA, which allows us to borrow up to \$100.0 million, with a maturity date of October 2026. We may require additional equity or debt financing to fund our operations and capital expenditures. Our ability to obtain financing will depend, among other things, on our

development efforts, business plans, operating performance and the condition of the capital markets at the time we seek financing. We cannot assure you that additional financing will be available to us on favorable terms if and when required, or at all.

We have and may in the future acquire other businesses or receive offers to be acquired, which could require significant management attention, disrupt our business, dilute stockholder value and adversely affect our operating results.

As part of our business strategy, we have and may in the future make investments in complementary businesses, products, services or technologies. These acquisitions and other transactions and arrangements involve significant challenges and risks, including not advancing our business strategy, receiving an unsatisfactory return on our investment, difficulty integrating and retaining new employees, business systems, and technology, or distracting management from our other business initiatives. If an arrangement fails to adequately anticipate changing circumstances and interests of a party, it may result in early termination or renegotiation of the arrangement. The success of these transactions and arrangements will depend in part on our ability to leverage them to enhance our existing products or develop compelling new ones. It may take longer than expected to realize the full benefits from these transactions and arrangements such as increased revenue or enhanced efficiencies, or the benefits may ultimately be smaller than we expected. These events could adversely affect our consolidated financial statements.

If we fail to maintain an effective system of internal controls in the future, we may experience a loss of investor confidence and an adverse impact to our stock price.

Pursuant to the Sarbanes-Oxley Act of 2002, we are required to document and test our internal control procedures and to provide a report by management on internal control over financial reporting, including management's assessment of the effectiveness of such control. We previously reported and remediated material weaknesses in internal control over financial reporting. Completion of remediation does not provide assurance that our remediation or other controls will continue to operate properly. If we are unable to maintain effective internal control over financial reporting or disclosure controls and procedures, our ability to record, process and report financial information accurately, and to prepare consolidated financial statements within required time periods could be adversely affected, which could subject us to litigation or investigations requiring management resources and payment of legal and other expenses, negatively affect investor confidence in our consolidated financial statements and adversely impact our stock price.

Item 2. Unregistered Sales of Equity Securities and Use of proceeds

Recent Sales of Unregistered Securities

None.

Issuer Purchases of Equity Securities

The following table presents information with respect to the Company's repurchase of common stock during the quarter ended December 31, 2022.

Period	Total Number of Shares Purchased ⁽¹⁾	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Approximate Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (in thousands)
Oct 2 - Oct 29	—	\$ —	—	\$ 100,000
Oct 30 - Nov 26	—	\$ —	—	\$ 100,000
Nov 27 - Dec 31	849,806	\$ 17.69	849,806	\$ 84,957
Total	<u>849,806</u>		<u>849,806</u>	

(1) In November 2022, the Board authorized a common stock repurchase program of up to \$100.0 million. During the three months ended December 31, 2022, the Company repurchased 849,806 shares for an aggregate purchase price of \$15.0 million at an average price of \$17.69 per share under the repurchase program. See Note 8. *Stockholders' Equity* of the Company's condensed consolidated financial statements for further information. Over the past three fiscal years, the Company has completed \$250.0 million in share repurchases, for 11,760,762 shares, at an average price of \$21.26 per share. The Company withholds shares of common stock from certain employees in connection with the vesting of stock awards issued to such employees to satisfy applicable tax withholding requirements. Although these withheld shares are not issued or considered common stock repurchases under the Company's stock repurchase program and therefore are not included in the preceding table, they are treated as common stock repurchases in the Company's financial statements as they reduce the number of shares that would have been issued upon vesting.

Item 3. Default Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

None.

Item 5. Other Information

None.

Item 6. Exhibit Index

Exhibit number	Exhibit title	Incorporated by reference				Filed or furnished herewith
		Form	File no.	Exhibit	Filing date	
31.1	Certification of Chief Executive Officer pursuant to Rules 13a-14(a) and Rule 15d-14(a) of the Exchange Act					X
31.2	Certification of Chief Financial Officer pursuant to Rules 13a-14(a) and Rule 15d-14(a) of the Exchange Act					X
32.1*	Certification of Chief Executive Officer pursuant to Rule 13a-14(b) of the Exchange Act and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002					X
32.2*	Certification of Chief Financial Officer pursuant to Rule 13a-14(b) of the Exchange Act and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002					X
101	The following financial statements from the Company's Quarterly Report on Form 10-Q for the quarter ended December 31, 2022, formatted in Inline XBRL: (i) Condensed consolidated balance sheets, (ii) Condensed consolidated statements of operations and comprehensive income, (iv) Condensed consolidated statements of stockholders' equity, (v) Condensed consolidated statements of cash flows and (vi) Notes to condensed consolidated financial statements, tagged as blocks of text and including detailed tags					X
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)					X

**The certifications furnished in Exhibits 32.1 and 32.2 hereto are deemed to accompany this Form 10-Q and are not deemed “filed” for purposes of Section 18 of the Exchange Act, or otherwise subject to the liability of that section, nor shall they be deemed incorporated by reference into any filing under the Securities Act or the Exchange Act.*

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this Quarterly Report on Form 10-Q to be signed on its behalf by the undersigned thereunto duly authorized.

Sonos, Inc.

Date: February 8, 2023

By: /s/ Patrick Spence

Patrick Spence
Chief Executive Officer and Director
(Principal Executive Officer)

Date: February 8, 2023

By: /s/ Eddie Lazarus

Eddie Lazarus
Chief Financial Officer and Chief Legal Officer
(Principal Financial Officer)

Date: February 8, 2023

By: /s/ Chris Mason

Chris Mason
SVP, Finance and Chief Accounting Officer
(Principal Accounting Officer)