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SONOS

Third Quarter Fiscal 2025
Conference Call Remarks
August 6, 2025 - 4:30 pm Eastern/1:30 pm Pacific

James Baglanis, Investor Relations

Good afternoon and welcome to Sonos' Third Quarter Fiscal 2025 earnings conference call. I am James Baglanis, and with me today are Sonos' CEO, Tom Conrad, CFO Saori Casey and Chief Legal and Business Development Officer, Eddie Lazarus.

Before I hand it over to Tom, I would like to remind everyone that today's discussion will include forward-looking statements regarding future events and our future financial performance. These statements reflect our views as of today only and should not be considered as representing our views of any subsequent date. These statements are also subject to material risks and uncertainties that could cause actual results to differ materially from expectations reflected in the forward-looking statements. A discussion of these risk factors is fully detailed under the caption “Risk Factors” in our filings with the SEC. During this call, we will also refer to certain non-GAAP financial measures. For information regarding our non-GAAP financials and a reconciliation of GAAP to non-GAAP measures, please refer to today's press release regarding our third quarter results posted to the Investor Relations portion of our website.

As a reminder, the press release, supplemental earnings presentation including our guidance, and conference call transcript will be available on our investor relations website, investors.sonos.com.

I will now turn the call over to Tom.

Tom Conrad, Chief Executive Officer

Thank you, James, and thanks to you all for joining us.

I’m speaking to you today not just as the new CEO of Sonos but as someone who deeply believes in what this company can be. I’ve devoted my career to building consumer products that people love and I took on this role because I believe Sonos is one of the few companies with the ingredients to do that at the highest level. There’s a reason I have a Sonos Ace tattoo on my forearm: I love this company, its mission and the possibilities ahead.

Over the past six months, I’ve had the chance to work closely with every part of the business. I’ve seen just how much our people care about the quality of our products, our customers’ experience, the craft of what we build and the operational rigor we bring to the task every day. Working with this incredible team has only deepened my conviction that Sonos can be among the most consequential hardware platform companies in the world.

That’s why I’m so honored the Board has asked me to lead Sonos into its next chapter and why I’m so optimistic about what comes next.

My appointment is not just a leadership transition. It is a turning point for the company, a return to our founding principles of obsessive craftsmanship, customer-first design, and category-defining innovation. We have a lot of work ahead of us to translate our convictions into a return to growth with better profitability and we’re approaching the challenge with urgency.

Now let me tell you why I’m so excited about the future.

First, the Sonos we’re building today is not just a product company; we are a platform company. A platform where our expanding portfolio of hardware products compound in value thanks to powerful software upgrades that deliver unique experiences for the home and beyond. This ecosystem connects not just our products but also our partners, developers, and consumers. Every new product, every software feature and every integration ensures that, over time, Sonos becomes more powerful, more interconnected and more irreplaceable in our customers' homes.

Second, Sonos has an extraordinary brand. We are the clear leader in wireless home audio, and we have earned that position by delivering consistently great sound, thoughtful industrial design, and a system that works across every room in the home. That’s not marketing spin, it is why we are the #1 home theater brand in the US and why our installer and channel partnerships remain so strong.

Third, we're making significant operational progress. Earlier this year, we reorganized to improve our product cadence while reducing our annual operating expenses by more than $100 million. This has catalyzed a focus on the things that matter: the core experience, profitable growth, and the kinds of innovations only Sonos can deliver. For example, this quarter we delivered new AI-powered voice enhancement features on Arc Ultra and state of the art adaptive noise cancelation for Sonos Ace. We're keeping this momentum as we build a strong roadmap that stretches through Fiscal 2026 and beyond.

Finally, there are many opportunities ahead for growth. Despite our market leadership, we've only captured a small fraction of the global market. We have room to add new households and grow our installed base in both our existing and key growth markets. What's more our installed base is a powerful asset itself and roughly 40 to 45 percent of annual product registrations come from existing households. And we're leaning into this by delivering experiences that get better as your system expands.

Which is just to say, we know we have to do more. We'll make Sonos more relevant to people's daily lives by expanding the experiences we deliver and making them even easier to enjoy. We'll be more assertive in the products we bring to market and more expressive in how we tell the Sonos story. We can reconnect more deeply with artists, with culture, and with the spirit of invention that has always been part of this company.

This is the Sonos I'm building. It will take some time to bring this reinvention to the market. But we will move with conviction and clarity of purpose, and the payoff will be clear over the medium to long term.

Now let me share a few comments about our performance in Q3 and the business environment in which we're operating. We had a solid quarter with revenue and Adjusted EBITDA at or above the top of our guidance. Our results reflect a tight focus on execution, which yielded dollar share gains in home theater in the US, and on efficiency, which drove continued year-over-year declines in our Operating Expenses.

With respect to our operations, like many companies, the most significant near-term challenge has been the uncertain tariff environment. As a reminder, short of a few accessories and our passive speaker partnership with Sonance, we do all of our US-bound manufacturing in Vietnam and Malaysia. We talked last quarter about the contingency planning we underwent to minimize the effect of tariffs on our business while also doing what we can to limit the downstream impact to our customers. With last week's news, the tariff rates we will be subject to going forward appear to be 20% for Vietnam and 19% for Malaysia.

We continue to work closely with our contract manufacturers and our channel partners to share tariff costs, though it has become clear that we will need to raise prices on certain products later this year. As these pricing changes land, we'll monitor consumer behavior closely, as well as competitive trends across our categories, and make adjustments in collaboration with our channel partners when and if necessary to ensure we're exploring every opportunity to optimize our respective top and bottom lines.

In conclusion, Sonos has the right to lead. We have the brand, the platform, the team, and the permission to define what great means for audio and entertainment in the home, on the go, and into the future. We lost some momentum in 2024. We're starting to get it back. And we're going to accelerate our pace from here.

Now let me turn things over to Saori.

Saori Casey, Chief Financial Officer
Thank you, Tom. Hi everyone.

We are pleased to deliver Q3 financial results that exceeded our expectations. Revenue of $345 million was above the high end of our guidance range driven by better than expected portables and component products.

Q3 revenue declined 13% year over year versus our guidance of down 22% to 14%. Excluding the impact of the launch of Ace last year, when we recognized the revenue from the channel fill, our revenue was down mid-single digits in Q3, slightly better than the first half of the year and better than the overall category trends. This was driven by Arc and Arc Ultra which grew on a year over year basis.

GAAP gross margin was 43.4%, near the midpoint of our guidance range. Non-GAAP gross margin was 44.7%. We incurred $2.1 million of tariff expenses in Q3, which was a 60 basis point impact on our reported gross margin. This is consistent with our guidance for under $3 million in Q3.

Q3 GAAP Operating Expenses were $153 million, down 15% year over year.

Non-GAAP Operating Expenses of $131 million were down 15% year over year and came in about $9 million below the low end of our guidance. On a normalized basis primarily for variable compensation, Non-GAAP Operating Expenses declined by 23%, as we saw a full quarter benefit of savings from the reduction in force announced last quarter as well as from many other cost optimization efforts we had set out last summer.

As for the year over year trends of each Non-GAAP Operating Expense category, Research and Development expenses decreased by 17% due to cost optimization efforts from the prior quarter. G&A expenses decreased by 16% driven by headcount and various cost optimization efforts initiated last year. Sales and Marketing expenses decreased by 13%, driven by higher marketing investment last year from the launch of Ace.

Adjusted EBITDA was positive $36 million, at the high end of our guidance range of $12 to $37 million due to higher revenue and lower operating expenses.

Year to date, revenue declined by 8% while GAAP gross margin came in at 43.7% and Non-GAAP at 45.2%. Our GAAP and non-GAAP operating expenses declined by 8% and 11%, respectively, on a reported basis and by 16% on a normalized basis. Adjusted EBITDA declined 4% year over year, better than our revenue performance due to our expense discipline.

Our balance sheet remains strong as our net cash balance increased by $30 million sequentially to end the quarter at $254 million, which includes $53 million of marketable securities as we hold some excess cash in short duration treasury bills. We also have a $100 million undrawn revolving credit facility at our disposal.

Q3 free cash flow was $33 million, an increase from negative $65 million last quarter. Capex was $5 million, down from $6 million last quarter. We paid $3.5 million of cash tariffs in Q3, a bit below the low end of our $5 to $10 million guidance due to lower than planned inventory purchase pull-forward.

Our period-end inventory balance decreased 17% sequentially to $115 million, primarily due to lower finished goods. On a year over year basis, this was a 25% decrease primarily due to lower component balances. Our inventory consists of $93 million of finished goods and $22 million of components.

As we noted last quarter, our near-term priority is navigating this dynamic and uncertain environment with ample liquidity to preserve operational flexibility. As a result, we paused our repurchase activities in Q3. Returning capital to shareholders remains a key pillar of our capital allocation framework, and we have $150 million remaining on our current share repurchase authorization available at our disposal.

Guidance

Turning to our guidance, the Q4 outlook we're providing today reflects the demand trends we have observed quarter-to-date and does not assume any material change in consumer purchasing behavior as a result of this highly dynamic global trade environment.

Revenue

We expect Q4 revenue to be in the range of $260 million to $290 million, up +2% to +14% year over year.

We are not guiding Q1 at this time, but I would note that due to the launch timing of Arc Ultra and Sub 4 in Q1 of Fiscal 2025, we have a difficult year over year comparison. Also, as Tom mentioned earlier, we will be raising prices on certain products later this year. We have carefully formulated our pricing plan in support of our goal to optimize for gross profit dollars, however, it is difficult to accurately predict how our new pricing and overall market demand may impact unit sales volumes in this dynamic environment.

If not for the uncertainty introduced by our contemplated pricing changes, we had been expecting that our year over year comparisons would improve from Q1 through the balance of Fiscal 2026.

Gross Margin and Tariff Impact

We expect our Q4 GAAP gross margin to be in the range of 42% to 44%, with non-GAAP gross margin in the range of 43.7% to 45.5%. Our gross margin guidance embeds our expectation that tariff expenses will be approximately $5 million in Q4, which is around a 180 basis point headwind to gross margin, mostly representing the previous 10% tariff rate as well as inventory on hand.

On a cash basis, we expect to pay $8 to 10 million in Q4, as we build inventory ahead of our holiday quarter. This estimate is lower than our previous $20 to $30 million estimate based on new tariff rates and the timing of the effective date.

And while we’re not guiding Q1 at this time, we expect our GAAP and non-GAAP gross margin will be above 40% for the quarter even with the newly announced tariff rates due to our mitigation actions.

Operating Expenses and Adjusted EBITDA

We expect Q4 GAAP Operating Expenses to be in the range of $150 million to $155 million, down 13% to 10% from $172 million in Q4 of last year.

We expect Non-GAAP Operating Expenses to be in the range of $130 million to $135 million, down 9% to 6% from $143 million in Q4 of last year and roughly flat sequentially. This decline is less than the 15% decline we saw in Q3 primarily due to lower variable compensation expenses in Q4 of last year. On a normalized basis, our guidance implies Non-GAAP Operating Expenses will decline by 23% to 20% from Q4 of last year.

Bringing it all together, we expect Q4 Adjusted EBITDA to be in the range of minus $10 million to positive $14 million, representing a margin of approximately -4% to +5% and an improvement from negative $22.6 million in Q4 of last year. Please note that the Adjusted EBITDA figures I just quoted include the $5 million tariff impact I outlined while discussing gross margin.

Our Q4 guidance implies that our full year Adjusted EBITDA will be between $116 million and $140 million, an increase of 8% to 30% year over year from $108 million in Fiscal 2024. Growing Adjusted EBITDA while topline declines between 7% to 5% is the direct result of our transformation efforts.

Positioning Sonos for the Long Term

This marks our 4th consecutive quarter of delivering on our top and bottom line guidance while we navigate through a volatile and uncertain macro environment, thanks to the dedication and hard work of our employees. We continue to work hard on our transformation efforts to improve our operational efficiency to drive profitability and enable investments for our future growth. We will provide more updates in future quarters.

Speaking of future growth, although our growth markets represent a small share of our revenue today, we remain encouraged by their growth performance that will be a key contributor to our growth in the years to come. We also continue to see tremendous opportunities to grow within our developed markets. We have been navigating a cyclical downswing in our categories for some time, and we are confident that we are well positioned when the cycle rebounds as we continue to invest in the core experience and build out the Sonos platform.

We are excited to have Tom officially as our CEO, as his appointment marks the beginning of a new chapter to capitalize on our brand and leadership in wireless audio. With only a small fraction of the global market captured so far, there is a vast opportunity to introduce the compounding value of the Sonos platform to new customers.

After the call, we will update our earnings slides to reflect our Q4 guidance and our revised tariff exposure expectations.

With that, I'd like to turn the call over for questions.

Question and Answer Session

Steve Frankel - Rosenblatt
Congratulations, Tom. Maybe just start with some high-level insights on how you think about new product introductions. Prior to your appointment, the company was pretty set on introducing a couple of new pieces of hardware per year. You seem to be emphasizing software. So should we think about software innovation being as important in terms of new products to drive growth as new hardware products?

Tom Conrad, Chief Executive Officer - Sonos
Sure. Thanks, and it's great to be on the call as the CEO for the first time. I continue to think that a cadence of 2 new products a year is an excellent outcome for Sonos and its customers. And so there's really no change in our ambition in that regard. I will say, though, that we are, as you know, in the process of navigating tremendous reinvention here at Sonos and it takes time to drive change. And the beauty of software is that you have shorter lead times and the benefits of upgrades to the software platform can appear more quickly. Hardware, of course, has much longer cycles.

And so while it's true that today, I think we have the strongest product portfolio in our history across every room of the home and beyond. Our attention to software reliability and core experience over the last 15 months has created a kind of lull in new hardware releases coming over the next couple of quarters. So in the short term, you will see us work hard to drive differentiation and experience improvements to support the current portfolio through software upgrades.

Having said all of that, we all here at Sonos remain incredibly excited about our product road map with great new product introductions that will pick up in the second half of 2026. So expect in terms of near-term execution, continuing to deliver excellence in core experience, driving new customer acquisition and repurchase, look to us to sharpen our ability to tell the Sonos story, as Saori described, expanding and promising new geographies, maturing our relationship with installer channels and driving success in the new categories we've entered recently like headphones.

Steve Frankel - Rosenblatt
Right. And Saori, the last couple of quarters, there's been a lot of discussion about reducing costs, and you've done a great job. Are we towards the end of that journey? Or do you think excluding tariffs, there's more costs you can take out of the business to drive margin improvement as volumes return?

Saori Casey, CFO - Sonos

Thank you, Steve. We are still on our journey of our -- as we've been calling it transformation, but really driving cost structure and cost efficiency to be able to invest for the future. So our work continues, and we'll be -- we hope to be able to share more in the future quarters.

Erik Woodring - Morgan Stanley

And same, Tom, you are clearly deserving of the role, and so congrats on becoming the permanent CEO. I would love to maybe, Tom, I realize that it's early and this is maybe a tough question to answer, but you guys last quarter communicated a strategy of kind of trying to widen your aperture from a pricing and promotion perspective to kind of get new households in the door. Obviously, once they come in, there's a very powerful flywheel. Now obviously, tariffs are kind of forcing your hand a bit from a pricing perspective.

Can you maybe just give us a little bit more detail or direction on exactly how you think about what products should be higher priced because of tariff, what products maybe you don't want to adjust pricing because of some of this pricing strategy? Just love to get a little bit more flavor of how you're thinking about pricing increases versus tariffs. And then I have a follow-up, please.

Tom Conrad, Chief Executive Officer - Sonos

I'm not sure that on this call, we're going to go into more detail about the specifics of the pricing changes that we're making beyond just saying that, of course, we're evaluating each of the products in the line, contemplating our sense of elasticity and effect on demand as we make pricing changes.

I think the best way to think about what we're trying to do here strategically is to craft a pricing plan that supports our goal of optimizing gross profit dollars. We certainly will be paying close attention to how our customers respond to these pricing changes as well as the competitive trends across the portfolio in our categories.

And then I'll just say, we really believe that our portfolio of hardware products deliver truly exceptional value that compounds over time, thanks to the kinds of software updates that deliver new experiences. Just this quarter, we shipped AI speech enhancement for Arc Ultra, multi-user swap for Ace in home theater, new room tuning capabilities for Ace. So our customers benefit from products that improve over time after their purchase. And we think that, that puts us in a good position as we have to modulate pricing relative to our competitors who are so often are delivering commodity experiences.

Erik Woodring - Morgan Stanley

Okay. Okay. Totally fair. Understood. And then I'd love as a follow-up, maybe just if you could kind of touch on the high-level kind of market backdrop as you see it today and maybe where you see it going, again, I realize there's a lot of variables that go into the forward look. But do you see the environment getting better? Is it deteriorating? Anything by geography that you would call out? Would just love to know kind of what's going on behind the scenes kind of outside of what you guys can actually control.

Tom Conrad, Chief Executive Officer - Sonos
Sure. It is -- continues to be the case that the category remains cyclically challenged coming off of COVID pull-in and weak housing data as just 2 headwinds. On the other hand, more people are consuming content at home than ever before. More people are subscribing to digital music and video streaming services than ever before. More people are interacting with technology through voice and conversational AI than ever before.

And I really think that in time, all of these trends are going to drive a return to growth for the category, and I think we're uniquely positioned to capture that growth when it returns. So we're working hard in this sort of cyclical downturn to drive share through strong execution in innovation. You see that with Arc Ultra driving year-over-year gains in home theater in the U.S. this quarter on the backs of the SoundMotion technology that we brought to market. And you'll continue to see us work hard in that lane while we wait for what we think is the inevitable return of category demand.

Erik Woodring - Morgan Stanley
Super thanks. And maybe just last question, and then I'll get back in the queue for you, Saori, and kind of a similar question to my predecessor, which is last quarter, you guys talked about $580 million to $600 million of non-GAAP OpEx as kind of your target annualized run rate. I think you are actually already below that right now if we kind of take fiscal '25 in totality.

And so I know you're not going to necessarily guide for fiscal '26, but is $580 million to $600 million still the target run rate? Is it below that? I'd love if you could just share a bit more context about kind of what that target is, if it has changed at all?

Saori Casey, CFO - Sonos
Thanks, Erik. Yes, we're still -- we continue to still work on our efforts to optimize our cost structure. Part of it, we obviously want to reinvest into the business for the future growth. And so we're not guiding to an FY '26 OpEx today. However, I do want to call out part of what I mentioned on the prepared remarks that the resulting impact to even FY '25 adjusted EBITDA, we expect to grow 8% to 30% year over year on our bottom line for this year and as you will recall, we had our reduction in force both last August as well as even a larger on in February. So we are not seeing a full year impact of those activities that we've taken place to improve our cost structure this year in FY '25 and we expect that to fully materialize into FY '26 as well. But again, we're balancing with where we want to invest for our future as well as flowing it through

to the bottom line, but we expect to continue to improve our profitability. And we believe this business can expand both top and the bottom line.

Brent Thill - Jefferies
This is Rayyana Matraji on for Brent Thill. Congrats, Tom. Can you speak to how Sonos is leveraging AI to enhance the product or app experience? And do you think this could be a meaningful differentiator or monetization driver over time?

Tom Conrad, Chief Executive Officer - Sonos
Let me start by talking just a little bit about what I think of as the sort of the fundamental strengths of the Sonos' capability. We have best-in-class sound quality and industrial design. We invented the multi-room architecture that's defined the standard for customers everywhere.

We have this incredibly broad portfolio of premium form factors for every room and beyond. And the power of this ecosystem is really the software platform that connects all of those products with our partners and developers and our customers in truly unique and differentiated ways.

And I think what you're touching on is why I'm so excited about where this platform can go from here. I think our hardware and software is incredibly well positioned to deliver the next generation of conversational AI experiences in the home.

So I think the way to think about it is that Sonos isn't and has never been a company that sells a loose collection of speakers. Today, we're building a next-generation platform that we think will define how people experience sound and interaction in the home for the next decade and beyond. And of course, as a footnote, I should say that the company operationally is being transformed by the use of AI technology across all of our departments from engineering, certainly through marketing and legal and customer experience.

So we have a really big vision for AI, both in terms of increasing our operation agility as well as delivering incredible one-of-a-kind experiences in our customers' homes.