

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

FORM 10-Q

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

For the quarterly period ended March 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: 1-16027



LANTRONIX, INC.
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of incorporation or organization)

33-0362767
(I.R.S. Employer Identification No.)

7535 Irvine Center Drive, Suite 100, Irvine, California
(Address of principal executive offices)

92618
(Zip Code)

(949) 453-3990
(Registrant's telephone number, including area code)

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

<u>Title of each class</u>	<u>Trading Symbol(s)</u>	<u>Name of each exchange on which registered</u>
Common Stock, \$0.0001 par value	LTRX	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, a 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 ☐
Non-accelerated filer ☒
Emerging Growth Company ☐

Accelerated filer ☐
Smaller reporting company ☒

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. ☐

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

As of April 29, 2022, there were 34,797,971 shares of the registrant's common stock outstanding.

LANTRONIX, INC.
FORM 10-Q
FOR THE QUARTERLY PERIOD ENDED
March 31, 2022

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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q for the three months ended March 31, 2022 (the “Report”) contains forward-looking statements within the meaning of the federal securities laws, which statements are subject to substantial risks and uncertainties. These forward-looking statements are intended to qualify for the safe harbor from liability established by the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical fact included in this Report, or incorporated by reference into this Report, are forward-looking statements. Throughout this Report, we have attempted to identify forward-looking statements by using words such as “may,” “believe,” “will,” “could,” “project,” “anticipate,” “expect,” “estimate,” “should,” “continue,” “potential,” “plan,” “forecasts,” “goal,” “seek,” “intend,” other forms of these words or similar words or expressions or the negative thereof. Additionally, statements concerning future matters such as our expected earnings, revenues, expenses and financial condition, our expectations with respect to the development of new products, expectations regarding the impact of the COVID-19 pandemic and other statements regarding matters that are not historical are forward-looking statements.

We have based our forward-looking statements on management’s current expectations and projections about trends affecting our business and industry and other future events. Although we do not make forward-looking statements unless we believe we have a reasonable basis for doing so, we cannot guarantee their accuracy. Forward-looking statements are subject to substantial risks and uncertainties that could cause our future business, financial condition, results of operations or performance to differ materially from our historical results or those expressed or implied in any forward-looking statement contained in this Report. Factors which could have a material adverse effect on our operations and future prospects or which could cause actual results to differ materially from our expectations include, but are not limited to, those set forth under “Risk Factors” in Item 1A of Part II of this Report, as such factors may be updated, amended or superseded from time to time by subsequent public filings with the Securities and Exchange Commission. In addition, actual results may differ as a result of additional risks and uncertainties of which we are currently unaware or which we do not currently view as material to our business.

You should read this Report in its entirety, together with the documents that we file as exhibits to this Report, with the understanding that our future results may be materially different from what we currently expect. The forward-looking statements we make speak only as of the date on which they are made. We expressly disclaim any intent or obligation to update any forward-looking statements after the date hereof to conform such statements to actual results or to changes in our opinions or expectations, except as required by applicable law or the rules of The Nasdaq Capital Market. If we do update or correct any forward-looking statements, investors should not conclude that we will make additional updates or corrections.

We qualify all of our forward-looking statements by these cautionary statements.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

LANTRONIX, INC. **UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS** (In thousands)

	March 31, 2022	June 30, 2021
Assets		
Current assets:		
Cash and cash equivalents	\$ 22,782	\$ 9,739
Accounts receivable, net	23,189	13,515
Inventories, net	33,166	15,059
Contract manufacturers' receivables	2,028	1,960
Prepaid expenses and other current assets	3,995	2,880
Total current assets	85,160	43,153
Property and equipment, net	2,333	1,577
Goodwill	18,757	15,810
Purchased intangible assets, net	16,037	9,355
Lease right-of-use assets	8,360	2,431
Other assets	332	240
Total assets	\$ 130,979	\$ 72,566
Liabilities and stockholders' equity		
Current liabilities:		
Accounts payable	\$ 15,510	\$ 9,122
Accrued payroll and related expenses	3,690	4,942
Current portion of long-term debt, net	1,671	1,472
Other current liabilities	12,468	7,328
Total current liabilities	33,339	22,864
Long-term debt, net	14,691	2,210
Other non-current liabilities	7,920	1,396
Total liabilities	55,950	26,470
Commitments and contingencies (Note 9)		
Stockholders' equity:		
Common stock	3	3
Additional paid-in capital	286,686	249,885
Accumulated deficit	(212,031)	(204,163)
Accumulated other comprehensive income	371	371
Total stockholders' equity	75,029	46,096
Total liabilities and stockholders' equity	\$ 130,979	\$ 72,566

See accompanying notes to unaudited condensed consolidated financial statements.

LANTRONIX, INC.
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2022	2021	2022	2021
Net revenue	\$ 32,324	\$ 17,108	\$ 93,710	\$ 50,839
Cost of revenue	18,708	9,390	53,191	27,886
Gross profit	13,616	7,718	40,519	22,953
Operating expenses:				
Selling, general and administrative	8,326	4,995	25,167	14,747
Research and development	4,483	2,519	12,834	7,540
Restructuring, severance and related charges	51	120	760	349
Acquisition-related costs	154	178	763	178
Fair value remeasurement of earnout consideration	1,203	—	2,462	—
Amortization of purchased intangible assets	1,479	754	4,112	2,515
Total operating expenses	15,696	8,566	46,098	25,329
Loss from operations	(2,080)	(848)	(5,579)	(2,376)
Interest expense, net	(303)	(77)	(1,277)	(244)
Loss on extinguishment of debt	(764)	—	(764)	—
Other income (expense), net	32	(224)	(25)	(183)
Loss before income taxes	(3,115)	(1,149)	(7,645)	(2,803)
Provision for income taxes	75	38	223	145
Net loss	\$ (3,190)	\$ (1,187)	\$ (7,868)	\$ (2,948)
Net loss per share - basic and diluted	\$ (0.09)	\$ (0.04)	\$ (0.25)	\$ (0.10)
Weighted-average common shares - basic and diluted	34,695	28,819	31,925	28,617

See accompanying notes to unaudited condensed consolidated financial statements.

LANTRONIX, INC.
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(In thousands)

Three Months Ended March 31, 2022

	Common Stock			Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income	Total Stockholders' Equity
	Shares	Amount					
Balance at December 31, 2021	34,644	\$ 3		\$ 284,976	\$ (208,841)	\$ 371	\$ 76,509
Shares issued pursuant to stock awards, net	154	—		98	—	—	98
Tax withholding paid on behalf of employees for restricted shares	—	—		—	—	—	—
Fair value of warrants to purchase common stock issued with bank credit facility	—	—		—	—	—	—
Share-based compensation	—	—		1,612	—	—	1,612
Net loss	—	—		—	(3,190)	—	(3,190)
Balance at March 31, 2022	34,798	\$ 3		\$ 286,686	\$ (212,031)	\$ 371	\$ 75,029

Three Months Ended March 31, 2021

	Common Stock			Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income	Total Stockholders' Equity
	Shares	Amount					
Balance at December 31, 2020	28,767	\$ 3		\$ 247,619	\$ (201,880)	\$ 371	\$ 46,113
Shares issued pursuant to stock awards, net	127	—		83	—	—	83
Tax withholding paid on behalf of employees for restricted shares	—	—		(145)	—	—	(145)
Share-based compensation	—	—		1,043	—	—	1,043
Net loss	—	—		—	(1,187)	—	(1,187)
Balance at March 31, 2021	28,894	\$ 3		\$ 248,600	\$ (203,067)	\$ 371	\$ 45,907

Nine Months Ended March 31, 2022

	Common Stock			Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income	Total Stockholders' Equity
	Shares	Amount					
Balance at June 30, 2021	29,088	\$ 3		\$ 249,885	\$ (204,163)	\$ 371	\$ 46,096
Shares issued pursuant to equity offering, net	4,700	—		32,593	—	—	32,593
Shares issued pursuant to stock awards, net	1,010	—		761	—	—	761
Tax withholding paid on behalf of employees for restricted shares	—	—		(1,646)	—	—	(1,646)
Fair value of warrants to purchase common stock issued with bank credit facility	—	—		500	—	—	500
Share-based compensation	—	—		4,593	—	—	4,593
Net loss	—	—		—	(7,868)	—	(7,868)
Balance at March 31, 2022	34,798	\$ 3		\$ 286,686	\$ (212,031)	\$ 371	\$ 75,029

Nine Months Ended March 31, 2021

	Common Stock			Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income	Total Stockholders' Equity
	Shares	Amount					
Balance at June 30, 2020	28,231	\$ 3		\$ 246,265	\$ (200,119)	\$ 371	\$ 46,520
Shares issued pursuant to stock awards, net	663	—		518	—	—	518
Tax withholding paid on behalf of employees for restricted shares	—	—		(719)	—	—	(719)
Share-based compensation	—	—		2,536	—	—	2,536
Net loss	—	—		—	(2,948)	—	(2,948)
Balance at March 31, 2021	28,894	\$ 3		\$ 248,600	\$ (203,067)	\$ 371	\$ 45,907

See accompanying notes to unaudited condensed consolidated financial statements.

LANTRONIX, INC.
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)

	Nine Months Ended March 31,	
	2022	2021
Operating activities		
Net loss	\$ (7,868)	\$ (2,948)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Share-based compensation	4,593	2,536
Depreciation and amortization	737	658
Amortization of purchased intangible assets	4,112	2,515
Amortization of manufacturing profit in acquired inventory associated with acquisitions	380	7
Loss on disposal of property and equipment	3	192
Amortization of deferred debt issuance costs	241	21
Fair value remeasurement of earnout consideration	2,462	–
Loss on extinguishment of debt	764	–
Changes in operating assets and liabilities, net of assets and liabilities acquired:		
Accounts receivable	(4,518)	(212)
Inventories	(10,657)	(1,305)
Contract manufacturers' receivable	(68)	(921)
Prepaid expenses and other current assets	(761)	(1,047)
Lease right-of-use assets	1,203	1,128
Other assets	(94)	(11)
Accounts payable	4,281	1,420
Accrued payroll and related expenses	(1,261)	(231)
Other liabilities	385	782
Net cash provided by (used in) operating activities	<u>(6,066)</u>	<u>2,584</u>
Investing activities		
Purchases of property and equipment	(1,138)	(665)
Cash payment for acquisitions, net of cash and cash equivalents acquired	(23,629)	–
Net cash used in investing activities	<u>(24,767)</u>	<u>(665)</u>
Financing activities		
Net proceeds from issuances of common stock	33,354	518
Tax withholding paid on behalf of employees for restricted shares	(1,646)	(719)
Net proceeds from issuance of debt	28,800	–
Payment of borrowings on term loan	(16,625)	(1,125)
Net proceeds from borrowing on line of credit	2,500	–
Payment of borrowings on line of credit	(2,500)	–
Payment of lease liabilities	(7)	(7)
Net cash provided by (used in) financing activities	<u>43,876</u>	<u>(1,333)</u>
Increase in cash and cash equivalents	13,043	586
Cash and cash equivalents at beginning of period	9,739	7,691
Cash and cash equivalents at end of period	<u>\$ 22,782</u>	<u>\$ 8,277</u>

See accompanying notes to unaudited condensed consolidated financial statements.

LANTRONIX, INC.
NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
MARCH 31, 2022

1. Overview, Basis of Presentation and Significant Accounting Policies

Overview

Lantronix, Inc., which we refer to herein as the Company, Lantronix, we, our, or us, is a global provider of software as a service (“SaaS”), engineering services, and hardware for Edge Computing, the Internet of Things (“IoT”), and Remote Environment Management (“REM”). Lantronix enables its customers to provide reliable and secure solutions while accelerating their time to market. Lantronix’s products and services dramatically simplify operations through the creation, development, deployment and management of customer projects at scale while providing quality, reliability and security.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements of Lantronix have been prepared in accordance with United States generally accepted accounting principles (“U.S. GAAP”) for interim financial information and in accordance with the instructions to Form 10-Q and Article 8 of Securities and Exchange Commission (“SEC”) Regulation S-X. Accordingly, they should be read in conjunction with the audited consolidated financial statements and notes thereto for the fiscal year ended June 30, 2021, included in our Annual Report on Form 10-K for the fiscal year ended June 30, 2021, which was filed with the SEC on August 27, 2021. The unaudited condensed consolidated financial statements contain all normal recurring accruals and adjustments that, in the opinion of management, are necessary to present fairly the consolidated financial position of Lantronix at March 31, 2022, the consolidated results of our operations for the three and nine months ended March 31, 2022 and our consolidated cash flows for the nine months ended March 31, 2022. All intercompany accounts and transactions have been eliminated.

Significant Accounting Policies

Use of Estimates

The preparation of condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Accounting measurements at interim dates inherently involve greater reliance on estimates than at year-end. The inputs into certain of these estimates and assumptions include the consideration of the economic impact of the COVID-19 pandemic. Actual results could differ materially from these estimates, and such differences could affect the results of operations reported in future periods. As the impact of the COVID-19 pandemic continues to develop, many of these estimates could require increased judgment and carry a higher degree of variability and volatility, and may change materially in future periods.

The results of operations for the three and nine months ended March 31, 2022 are not necessarily indicative of the results to be expected for the full year or any future interim periods.

Reclassifications

Certain reclassifications have been made to the prior fiscal year financial information to conform with the current fiscal year presentation.

Recent Accounting Pronouncements

Revenue Contracts

In October 2021, the Financial Accounting Standards Board (“FASB”) issued an Accounting Standards Update (“ASU”) to improve the accounting for acquired revenue contracts with customers in a business combination by addressing diversity and inconsistency related to i) recognition of an acquired contract liability and ii) payment terms and their effect on subsequent revenue recognized by the acquirer. The amendments in this ASU require that an entity (acquirer) recognize and measure contract assets and contract liabilities acquired in a business combination in accordance with existing revenue recognition guidance under Accounting Standard Codification Topic (“ASC”) 606. At the acquisition date, an acquirer would assess how the acquiree applied ASC 606 to determine what to record for the acquired revenue contracts. Generally, this would result in an acquirer recognizing and measuring the acquired contract assets and contract liabilities consistent with how they were recognized and measured in the acquiree’s financial statements. The ASU is effective for Lantronix beginning in the first quarter of fiscal year 2024, however early adoption is permitted.

Current Expected Credit Losses

In June 2016, the FASB issued a new ASU requiring financial assets measured at amortized cost be presented at the net amount expected to be collected, through an allowance for credit losses that is deducted from the amortized cost basis. The ASU eliminates the threshold for initial recognition in current U.S. GAAP and reflects an entity’s current estimate of all expected credit losses. The measurement of expected credit losses is based on historical experience, current conditions, and reasonable and supportable forecasts that affect the collectability of the financial assets. The ASU is effective for Lantronix beginning in the first quarter of fiscal year 2024. The adoption of this guidance is not expected to have a material effect on our consolidated financial statements.

2. Revenue

Revenue is recognized upon the transfer of control of promised products or services to customers in an amount that reflects the consideration we expect to receive in exchange for those products or services. We apply the following five-step approach in determining the amount and timing of revenue to be recognized: (i) identifying the contract with a customer, (ii) identifying the performance obligations in the contract, (iii) determining the transaction price, (iv) allocating the transaction price to the performance obligations in the contract and (v) recognizing revenue when the performance obligation is satisfied. On occasion we enter into contracts that can include various combinations of products and services, which are generally capable of being distinct and accounted for as separate performance obligations.

Revenue is recognized net of (i) any taxes collected from customers, which are subsequently remitted to governmental authorities and (ii) shipping and handling costs collected from customers.

Products

Most of our product revenue is recognized as a distinct single performance obligation when products are tendered to a carrier for delivery, which represents the point in time that our customer obtains control of the promised products. A smaller portion of our product revenue is recognized when our customer receives delivery of the promised products.

A significant portion of our products are sold to distributors under agreements which contain (i) limited rights to return unsold products and (ii) price adjustment provisions, both of which are accounted for as variable consideration when estimating the amount of revenue to recognize. We base our estimates for returns and price adjustments primarily on historical experience; however, we also consider contractual allowances, approved pricing adjustments and other known or anticipated returns and price adjustments in a given period. Such estimates are generally made at the time of shipment to the customer and updated at the end of each reporting period as additional information becomes available and only to the extent that it is probable that a significant reversal of any incremental revenue will not occur. Our estimates of accrued variable consideration are included in other current liabilities in the accompanying unaudited condensed consolidated balance sheets.

Services

Revenues from our extended warranty and related services are generally recognized ratably over the applicable service period. Although not significant to date, revenues from sales of our SaaS solutions are recognized ratably over the applicable service period as well.

We derive a portion of our revenues from engineering and related consulting service contracts with customers. Revenues from professional engineering services are generally recognized as services are performed. These contracts generally include performance obligations in which control is transferred over time because the customer either simultaneously receives and consumes the benefits provided or our performance on the contract creates or enhances an asset that the customer controls. These contracts typically provide services on the following basis:

- Time & Materials ("T&M") – services consist of revenues from software modification, consulting implementation, training and integration services. These services are set forth separately in the contractual arrangements such that the total price of the customer arrangement is expected to vary depending on the actual time and materials incurred based on the customer's needs.
- Fixed Price – arrangements to render specific consulting and software modification services which tend to be more complex.

Performance obligations for T&M contracts qualify for the "Right to Invoice" practical expedient within the revenue guidance. Under this practical expedient, we may recognize revenue, over time, in the amount to which we have a right to invoice. In addition, we are not required to estimate variable consideration upon inception of the contract and reassess the estimate each reporting period. We have determined that this method best represents the transfer of services as, upon billing, we have a right to consideration from a customer in an amount that directly corresponds with the value to the customer of our performance completed to date.

We recognize revenue on fixed price contracts, over time, using an input method based on the proportion of our actual costs incurred (generally labor hours expended) to the total costs expected to complete the contract performance obligation. We determined that this method best represents the transfer of services as the proportion closely depicts the efforts or inputs completed towards the satisfaction of a fixed price contract performance obligation.

Multiple Performance Obligations

From time to time, we may enter into contracts with customers that include promises to transfer multiple deliverables that may include sales of products, professional engineering services and other product qualification or certification services. Determining whether the deliverables in such arrangements are considered distinct performance obligations that should be accounted for separately versus together often requires judgment. We consider performance obligations to be distinct when the customer can benefit from the promised good or service on its own or by combining it with other resources readily available and when the promised good or service is separately identifiable from other promised goods or services in the contract. In such arrangements, we allocate revenue on a relative standalone selling price basis by maximizing the use of observable inputs to determine the standalone selling price for each performance obligation.

Net Revenue by Product Line and Geographic Region

We organize our products and solutions into three product lines: IoT, REM and Other. Our IoT products typically connect to one or more existing machines or are built into new industrial devices to provide network connectivity. Our REM product line includes out-of-band management, console management, power management, and IP connected keyboard-video-mouse (commonly referred to as "IPKVM") products that provide remote access to Information Technology ("IT") and networking infrastructure deployed in test labs, data centers, branch offices and server rooms. We categorize products that are non-focus or end-of-life as Other.

We conduct our business globally and manage our sales teams by three geographic regions: the Americas; Europe, Middle East, and Africa (“EMEA”); and Asia Pacific Japan (“APJ”).

The following tables present our net revenue by product line and by geographic region. Net revenues by geographic region are based on the “bill-to” location of our customers:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2022	2021	2022	2021
	(In thousands)			
IoT	\$ 28,587	\$ 13,661	\$ 79,939	\$ 41,683
REM	3,614	3,305	13,357	8,802
Other	123	142	414	354
	<u>\$ 32,324</u>	<u>\$ 17,108</u>	<u>\$ 93,710</u>	<u>\$ 50,839</u>

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2022	2021	2022	2021
	(In thousands)			
Americas	\$ 20,448	\$ 8,615	\$ 58,748	\$ 27,567
EMEA	5,071	4,096	15,481	11,475
Asia Pacific Japan	6,805	4,397	19,481	11,797
	<u>\$ 32,324</u>	<u>\$ 17,108</u>	<u>\$ 93,710</u>	<u>\$ 50,839</u>

The following table presents product revenues and service revenues as a percentage of our total net revenue:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2022	2021	2022	2021
Product revenues	94%	93%	94%	96%
Service revenues	6%	7%	6%	4%

Service revenue is comprised primarily of professional services, software license subscriptions, and extended warranties.

Contract Balances

In certain instances, the timing of revenue recognition may differ from the timing of invoicing to our customers. We record a contract asset receivable when revenue is recognized prior to invoicing, and a contract or deferred revenue liability when revenue is recognized subsequent to invoicing. With respect to product shipments, we expect to fulfill contract obligations within one year and so we have elected not to separately disclose the amount nor the timing of recognition of these remaining performance obligations. For contract balances related to contracts that include services and multiple performance obligations, refer to the deferred revenue discussion below.

Deferred Revenue

Deferred revenue is primarily comprised of unearned revenue related to our extended warranty services and certain software services. These services are generally invoiced at the beginning of the contract period and revenue is recognized ratably over the service period. Current and non-current deferred revenue balances represent revenue allocated to the remaining unsatisfied performance obligations at the end of a reporting period and are respectively included in other current liabilities and other non-current liabilities in the accompanying unaudited condensed consolidated balance sheets.

The following table presents the changes in our deferred revenue balance for the nine months ended March 31, 2022 (in thousands):

Balance, June 30, 2021	\$	1,091
New performance obligations		1,004
Performance obligations acquired from acquisition		42
Recognition of revenue from satisfying performance obligations		(828)
Balance, March 31, 2022		1,309
Less: non-current portion of deferred revenue		(354)
Current portion, March 31, 2022	\$	<u>955</u>

We currently expect to recognize substantially all of the non-current portion of deferred revenue over the next 2 to 4 years.

3. Acquisition

On April 28, 2021, we entered into a Securities Purchase Agreement (the “Purchase Agreement”) with Communications Systems, Inc., a Minnesota corporation (“CSI”), pursuant to which we agreed to purchase from CSI the Transition Networks (“TNI”) and Net2Edge businesses of CSI (the “Transaction”). The Transaction closed on August 2, 2021 (the “Closing Date”), with Lantronix acquiring all outstanding shares of the common stock of TNI and all of the outstanding ordinary shares of Transition Networks Europe Limited (such entity, together with TNI, the “TN Companies”) for an aggregate purchase price of up to approximately \$32,028,000 consisting of (i) \$25,028,000 cash to be paid on the Closing Date, plus (ii) earnout payments of up to \$7,000,000, payable following two successive 180-day intervals after the Closing Date based on revenue targets for the business of the TN Companies as specified in the Purchase Agreement, subject to certain adjustments and allocations as further described in the Purchase Agreement. Based on preliminary working capital estimates of the TN Companies at the Closing Date, we paid \$24,160,000 in cash consideration on the Closing Date. In September 2021, pursuant to working capital adjustments as outlined in the Purchase Agreement, the net cash consideration paid as of the Closing Date was adjusted to approximately \$23,651,000.

Concurrently with the closing of the Transaction, CSI and Lantronix entered in a Transition Services Agreement under which CSI will perform administrative and IT services, and lease office, warehouse and production space to Lantronix for the TN Companies for a period of up to twelve months.

The acquisition of the TN Companies provides Lantronix with complementary IoT connectivity products and capabilities, including switching, power over ethernet and media conversion and adapter products.

A summary of the purchase consideration for the TN Companies is as follows (in thousands):

Cash consideration paid to CSI	\$	23,651
Estimated fair value of earnout consideration		393
Total purchase consideration	\$	<u>24,044</u>

We recorded the TN Companies’ tangible and intangible assets and liabilities based on their estimated fair values as of the Closing Date and allocated the remaining purchase consideration to goodwill. Our valuation assumptions of acquired assets and assumed liabilities require significant estimates, especially with respect to intangible assets. Updates to the valuation of certain assets acquired and liabilities assumed, including our evaluation of certain income tax positions, may result in changes to the recorded amounts of assets and liabilities, with corresponding adjustments to goodwill in subsequent periods. We expect to complete the purchase price allocation within 12 months of the Closing Date.

In December 2021, based on additional analysis and refinements to our estimates, we adjusted the preliminary purchase price allocation as of the Closing Date to (i) increase the estimated fair value of earnout consideration by \$47,000 and (ii) decrease amortizable intangible assets by \$440,000. These adjustments resulted in a net offsetting increase to goodwill of \$487,000. We do not believe these adjustments had a material effect on our consolidated financial statements.

The updated purchase price allocation is as follows (in thousands):

Cash and cash equivalents	\$	22
Accounts receivable, net		5,156
Inventories, net		7,830
Prepaid expense and other current assets		355
Property and equipment, net		121
Goodwill		2,947
Amortizable intangible assets		10,794
Accounts payable		(1,872)
Accrued Payroll		(9)
Other current liabilities		(1,300)
Total consideration	\$	<u>24,044</u>

The factors that contributed to a purchase price resulting in the recognition of goodwill include our belief that the Transaction will create a more diverse IoT company with respect to product offerings and our belief that we are committed to improving cost structures in accordance with our operational and restructuring plans which should result in a realization of cost savings and an improvement of overall efficiencies.

Depending on the structure of a particular acquisition, goodwill and identifiable intangible assets may not be deductible for tax purposes. We have determined that goodwill and identifiable intangible assets related to the Transaction are not deductible.

Acquisition-related costs were expensed in the periods in which the costs were incurred.

The valuation of identifiable intangible assets and their estimated useful lives are as follows:

	<u>Asset Fair Value</u> <u>(In thousands)</u>	<u>Weighted Average</u> <u>Useful Life</u> <u>(In years)</u>
Customer relationships	\$ 7,467	3.5
Developed technology	1,890	3.5
Order backlog	567	1.0
Trademarks and trade names	870	2.0

The intangible assets are amortized on a straight-line basis over the estimated weighted-average useful lives.

Valuation Methodology

The customer relationships and order backlog were valued using the multi-period excess earnings method, which estimates revenues and cash flows derived from this asset and also considers portions of the cash flows that can be attributed to the use of other supporting assets. The useful lives of customer relationships are estimated based primarily upon customer turnover data. Order backlog was estimated to be substantially fulfilled within a year of the Closing Date.

Developed technology and trademarks and trades names were valued using the relief-from-royalty method. This method is an income approach that estimates the portion of a company's earnings attributable to an asset based on the royalty rate the company would have paid for the use of the asset if it did not own it. Royalty payments are estimated by applying a royalty rate to the prospective revenue attributable to the intangible asset. The resulting annual royalty payments are tax-affected and then discounted to present value.

Assumptions used in forecasting cash flows for each of the identified intangible assets included consideration of the following:

- Historical performance including sales and profitability
- Business prospects and industry expectations
- Estimated economic life of the asset
- Development of new technologies
- Acquisition of new customers
- Attrition of existing customers
- Obsolescence of technology over time

The fair value of earnout consideration was estimated based on applying a Monte Carlo simulation method to forecast achievement of the revenue targets. This method involves many possible value outcomes which are evaluated to establish an estimated value. Key inputs in the valuation include forecasted revenue, revenue volatility and discount rate.

Remeasurement of Earnout Consideration

During the three months ended March 31, 2022, we remeasured the estimated fair value of the earnout consideration to a total of \$2,855,000 based on the achievement of certain revenue targets for the business of the TN Companies during the first and second 180-day intervals after the Closing Date. As compared to the previously recorded estimate of \$1,652,000, this resulted in an upward adjustment of \$1,203,000 that was recorded within our operating expenses in the accompanying unaudited condensed consolidated statements of operations.

Additionally, the accompanying unaudited condensed consolidated statement of operations for the nine months ended March 31, 2022 includes an adjustment of \$1,259,000 that was recorded in the prior quarter based on our expectations as of December 31, 2021 of achieving revenue targets of the business of the TN Companies.

Supplemental Pro Forma Information

The following supplemental pro forma data summarizes our results of operations for the periods presented, as if we completed the acquisition of the TN Companies as of the first day of our fiscal year ended June 30, 2021. The supplemental pro forma data reports actual operating results adjusted to include the pro forma effect and timing of the impact of amortization expense of identified intangible assets, restructuring costs, the purchase accounting effect on inventories acquired, and transaction costs. In accordance with the pro forma acquisition date, we recorded in the nine months ended March 31, 2021 supplemental pro forma data (i) cost of goods sold from manufacturing profit in acquired inventory of \$380,000, (ii) acquisition related restructuring costs of \$507,000 and (iii) acquisition-related costs of \$609,000, with a corresponding reduction in the nine months ended March 31, 2022 supplemental pro forma data. Additionally, we recorded \$2,757,000 of amortization expense in the nine months ended March 31, 2021 supplemental pro forma data, and additional amortization expense of \$52,000 in the nine months ended March 31, 2022 supplemental pro forma data to represent amortization for the full fiscal year-to-date period.

Net sales related to products from the acquisition of the TN Companies contributed slightly over 28% of our total net sales for the nine months ended March 31, 2022. As of the Closing Date, we began to immediately integrate the acquisition into existing operations, engineering groups, sales distribution networks and management structure, making it generally impracticable to determine the post-acquisition net sales and earnings on a standalone basis.

Supplemental pro forma data is as follows:

	Nine Months Ended March 31,	
	2022	2021
	(In thousands, except per share amounts)	
Pro forma net revenue	\$ 96,497	\$ 76,877
Pro forma net loss	\$ (6,432)	\$ (5,545)
Pro forma net loss per share:		
Basic and Diluted	\$ (0.20)	\$ (0.19)

4. Supplemental Financial Information

Inventories

Inventories are stated at the lower of cost (first-in, first-out) or net realizable value and consist of the following:

	March 31, 2022	June 30, 2021
	(In thousands)	
Finished goods	\$ 17,448	\$ 7,738
Raw materials	15,718	7,321
Inventories	<u>\$ 33,166</u>	<u>\$ 15,059</u>

Other Liabilities

The following table presents details of our other liabilities:

	March 31, 2022	June 30, 2021
	(In thousands)	
Current		
Accrued variable consideration	\$ 2,092	\$ 1,347
Customer deposits and refunds	1,023	1,133
Accrued raw materials purchases	281	176
Deferred revenue	955	850
Lease liability	861	1,174
Taxes payable	442	388
Warranty reserve	635	197
Other accrued operating expenses	6,179	2,063
Total other current liabilities	<u>\$ 12,468</u>	<u>\$ 7,328</u>
Non-current		
Lease liability	\$ 7,566	\$ 1,155
Deferred revenue	354	241
Total other non-current liabilities	<u>\$ 7,920</u>	<u>\$ 1,396</u>

Computation of Net Loss per Share

Basic and diluted net loss per share is calculated by dividing net loss by the weighted-average number of common shares outstanding during the applicable period.

The following table presents the computation of net loss per share:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2022	2021	2022	2021
	(In thousands, except per share data)			
Numerator:				
Net loss	<u>\$ (3,190)</u>	<u>\$ (1,187)</u>	<u>\$ (7,868)</u>	<u>\$ (2,948)</u>
Denominator:				
Weighted-average common shares outstanding - basic and diluted	<u>34,695</u>	<u>28,819</u>	<u>31,925</u>	<u>28,617</u>
Net loss per share - basic and diluted	<u>\$ (0.09)</u>	<u>\$ (0.04)</u>	<u>\$ (0.25)</u>	<u>\$ (0.10)</u>

The following table presents the common stock equivalents excluded from the diluted net loss per share calculation, because they were anti-dilutive for the periods presented. These excluded common stock equivalents could be dilutive in the future.

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2022	2021	2022	2021
	(In thousands)			
Common stock equivalents	1,175	745	1,154	937

Purchased Intangible Assets

The following table presents details of purchased intangible assets:

	March 31, 2022			June 30, 2021		
	Gross Carrying Amount	Accumulated Amortization	Net Book Value	Gross Carrying Amount	Accumulated Amortization	Net Book Value
	(In thousands)					
Developed technology	\$ 5,731	\$ (2,170)	\$ 3,561	\$ 3,841	\$ (1,249)	\$ 2,592
Customer relationships	16,498	(4,796)	11,702	9,030	(2,267)	6,763
Order backlog	1,406	(1,214)	192	840	(840)	—
Non-compete agreements	400	(400)	—	400	(400)	—
Trademark and trade name	1,245	(663)	582	375	(375)	—
	<u>\$ 25,280</u>	<u>\$ (9,243)</u>	<u>\$ 16,037</u>	<u>\$ 14,486</u>	<u>\$ (5,131)</u>	<u>\$ 9,355</u>

We do not currently have any purchased intangible assets with indefinite useful lives.

As of March 31, 2022, future estimated amortization expense is as follows:

Years Ending June 30,

(In thousands)

2022 (remainder)	\$ 1,478
2023	5,400
2024	4,952
2025	3,358
2026	849
	<u>\$ 16,037</u>

Restructuring, Severance and Related Charges

The following table presents details of the liability we recorded related to restructuring, severance and related activities:

	Nine Months Ended March 31, 2022
	(In thousands)
Beginning balance	\$ 88
Charges	760
Payments	(843)
Ending balance	<u>\$ 5</u>

The ending balance is recorded in accrued payroll and related expenses in the accompanying unaudited condensed consolidated balance sheet at March 31, 2022.

Supplemental Cash Flow Information

The following table presents non-cash investing transactions excluded from the accompanying unaudited condensed consolidated statements of cash flows:

	Nine Months Ended March 31,	
	2022	2021
	(In thousands)	
Accrued property and equipment paid for in the subsequent period	\$ 235	\$ 40
Fair value of warrant to purchase common stock issued with bank credit facility	\$ 500	\$ —
Fair value of earnout consideration from TNI acquisition at the Closing Date	<u>\$ 393</u>	<u>\$ —</u>

5. Warranty Reserve

The standard warranty periods we provide for our products typically range from one to five years. The majority of products acquired through the acquisition of the TN Companies carry a limited lifetime warranty, which requires us to repair or replace a defective product, or offer a refund of a portion of the purchase price based on a depreciated value at our option. We establish reserves for estimated product warranty costs at the time revenue is recognized based upon our historical warranty experience, and for any known or anticipated product warranty issues.

The following table presents details of our warranty reserve, which is included in other current liabilities in the unaudited condensed consolidated balance sheet:

	Nine Months Ended March 31, 2022	Year Ended June 30, 2021
	(In thousands)	
Beginning balance	\$ 197	\$ 181
Warranty reserve assumed from acquisition of TN Companies	483	—
Charged to cost of revenue	167	226
Usage	(212)	(210)
Ending balance	<u>\$ 635</u>	<u>\$ 197</u>

6. Bank Loan Agreements

In connection with the Transaction on the Closing Date (refer to *Note 3*), we entered into (i) a Third Amended and Restated Loan and Security Agreement with Silicon Valley Bank (“SVB”), pursuant to which SVB made a term loan of \$17,500,000 on the Closing Date and made available a revolving credit facility of up to \$2,500,000 (the term loan facility and the revolving credit facility, the “Senior Credit Facilities”) and (ii) Mezzanine Loan and Security Agreement with SVB Innovation Credit Fund VIII, L.P. (“Lender”), pursuant to which Lender funded on the Closing Date a \$12,000,000 term loan facility (the “Mezzanine Credit Facility”). As part of the Mezzanine Credit Facility, we issued the Lender two warrants, each to purchase approximately 64,000 shares of our common stock at a price per share of \$4.695. The estimated fair value of the warrants was recorded to stockholders’ equity with the offset recorded as a discount against the Mezzanine Credit Facility debt balance. Substantially all of our tangible and intangible assets are pledged as collateral against these credit facilities.

The proceeds of the Senior Credit Facilities were used to refinance our outstanding obligations owing to SVB under our prior Second Amended and Restated Loan and Security Agreement with SVB, and the remaining proceeds of the Senior Credit Facilities and the proceeds from the Mezzanine Credit Facility were used to fund the purchase price of the TN Companies, to pay related fees and expenses, and also separately for working capital and general corporate purposes.

The Senior Credit Facilities mature on August 2, 2025 and the Mezzanine Credit Facility matures on February 2, 2026. Advances under the Senior Credit Facilities bore interest at LIBOR or the Prime Rate, at the option of Lantronix, plus a margin that ranged from 3.00% to 4.00% in the case of LIBOR and 1.50% to 2.50% in the case of the Prime Rate, depending on our total leverage with a LIBOR floor of 0.50% and a Prime Rate floor of 3.25%. Advances under the Mezzanine Credit Facility bore interest at LIBOR or the Prime Rate, at the option of Lantronix, plus a margin of 9.00% with a floor of 1.00% in the case of LIBOR and a margin of 7.50% with a floor of 3.50% in the case of the Prime Rate. We are also obligated to pay other customary facility fees for credit facilities of similar size and type.

In January 2022, we terminated the Mezzanine Credit Facility with the Lender, for which we repaid a total of \$12,152,500 to pay off the Mezzanine Credit Facility in full. There was no requirement to pay a termination fee. Pursuant to the applicable accounting guidance, we recognized a non-cash loss on the extinguishment of this debt of \$764,000, representing the write-off of unamortized deferred financing costs. This was recorded in Loss on extinguishment of debt in the accompanying condensed consolidated statements of operations for the three and nine months ended March 31, 2022.

In February 2022, we entered into an amendment to our Senior Credit Facilities which (i) increased the amount available under the revolving credit facility from \$2,500,000 to \$7,500,000, (ii) removed and replaced LIBOR benchmark provisions with Term Secured Overnight Financing Rate (“SOFR”) benchmark provisions and (iii) provided that advances under the Senior Credit Facilities bear interest at Term SOFR or the Prime Rate, at the option of Lantronix, plus a margin that ranges from 3.10% to 4.10% in the case of Term SOFR and 1.50% to 2.50% in the case of the Prime Rate, depending on our total leverage with a Term SOFR floor of 0.00% and a Prime Rate floor of 3.25%. We paid a nonrefundable fee of \$25,000 in connection with this amendment to our Senior Credit Facilities.

The following table summarizes our outstanding debt:

	March 31, 2022	June 30, 2021
	(In thousands)	
Outstanding borrowings on credit facilities	\$ 16,625	\$ 3,750
Less: Unamortized debt issuance costs	(263)	(68)
Net Carrying amount of debt	16,362	3,682
Less: Current portion	(1,671)	(1,472)
Non-current portion	<u>\$ 14,691</u>	<u>\$ 2,210</u>

During the three and nine months ended March 31, 2022, we recognized \$290,000 and \$1,210,000 of interest expense, respectively, in the accompanying unaudited condensed consolidated statements of operations related to interest and amortization of debt issuance associated with the borrowings under the Senior Credit Facilities and Mezzanine Credit Facility.

Financial Covenants

The Senior Credit Facilities and Mezzanine Credit Facility require Lantronix to comply with a minimum liquidity test, a maximum leverage ratio and a minimum fixed charge coverage ratio. We are currently in compliance with all financial covenants.

Liquidity

The Senior Credit Facilities and Mezzanine Credit Facility require that we maintain a minimum liquidity of \$5,000,000 and \$3,000,000, respectively, at SVB, as measured at the end of each month.

Maximum leverage ratio

The Senior Credit Facilities require that we maintain a maximum leverage ratio, calculated as the ratio of funded debt to the consolidated trailing 12 month earnings before interest, taxes, depreciation and amortization, and certain other allowable exclusions of (i) 2.50 to 1.00 for each calendar quarter ending June 30, 2021 through and including September 30, 2022, (ii) 2.25 to 1.00 for each calendar quarter ending December 31, 2022 through and including September 30, 2023, and (iii) 2.00 to 1.00 for the calendar quarter December 31, 2023 and each calendar quarter thereafter. The Mezzanine Credit Facility required that we maintain a maximum leverage ratio, calculated as the ratio of funded debt to the consolidated trailing 12 month earnings before interest, taxes, depreciation and amortization, and certain other allowable exclusions of (i) 4.25 to 1.00 for each calendar quarter ending June 30, 2021 through and including March 31, 2022, (ii) 3.75 to 1.00 for each calendar quarter ending June 30, 2022 through and including March 31, 2023, and (iii) 3.50 to 1.00 for the calendar quarter June 30, 2023 and each calendar quarter thereafter.

Minimum fixed charge coverage ratio

The Senior Credit Facilities require that we maintain a minimum fixed charge coverage ratio, calculated as the ratio of consolidated trailing 12 month earnings before interest, taxes, depreciation and amortization, and certain other allowable exclusions, less capital expenditures and taxes paid, to the trailing twelve month principal and interest payments on all funded debt of 1.25 to 1.00 as measured at the end of each calendar quarter. The Mezzanine Credit Facility required that we maintain a minimum fixed charge coverage ratio, calculated as the ratio of consolidated trailing 12 month earnings before interest, taxes, depreciation and amortization, and certain other allowable exclusions, less capital expenditures and taxes paid, to the trailing twelve month principal and interest payments on all funded debt of 1.10 to 1.00 as measured at the end of each calendar quarter.

In addition, both the Senior Credit Facilities and the Mezzanine Credit Facility contain customary representations and warranties, affirmative and negative covenants, including covenants that limit or restrict Lantronix and its subsidiaries' ability to incur liens, incur indebtedness, dispose of assets, make investments, make certain restricted payments, merge or consolidate and enter into certain speculative hedging arrangements. The Senior Credit Facilities and Mezzanine Credit Facility include a number of events of default, including, among other things, non-payment defaults, covenant defaults, cross-defaults to other materials indebtedness, bankruptcy and insolvency defaults and material judgment defaults. If any event of default occurs (subject, in certain instances, to specified grace periods), the principal, premium, if any, interest and any other monetary obligations on all the then outstanding amounts under the Senior Credit Facilities and Mezzanine Credit Facility may become due and payable immediately.

7. Stockholders' Equity

Public Offering

On November 18, 2021, we entered into an underwriting agreement (the "Underwriting Agreement") with TL Investment GmbH ("TL Investment") and Canaccord Genuity LLC, as representative of the several underwriters named therein (together, the "Underwriters"), relating to the Company's offer and sale of 4,700,000 shares (the "Firm Shares") of our common stock at an initial price to the public of \$7.50 per share. In addition, TL Investment granted the Underwriters a 30-day option to purchase up to an additional 705,000 shares (the "Option Shares") of our common stock held by TL Investment at the public offering price, less the underwriting discounts. On November 18, 2021, the Underwriters exercised their option to purchase the Option Shares from TL Investment in full. On November 22, 2021, we issued and delivered the Firm Shares and TL Investment delivered the Option Shares.

Net proceeds to Lantronix from the offering of the Firm Shares, after deducting the underwriting discount and offering expenses, were approximately \$32,600,000.

Stock Options

The following table presents a summary of activity during the nine months ended March 31, 2022 with respect to our stock options:

	Number of Shares	Weighted- Average Exercise Price per Share
	(In thousands)	
Balance of options outstanding at June 30, 2021	1,697	\$ 2.98
Granted	111	5.65
Expired	(14)	2.21
Exercised	(270)	2.04
Balance of options outstanding at March 31, 2022	1,524	\$ 3.35

Restricted Stock Units (RSUs)

The following table presents a summary of activity during the nine months ended March 31, 2022 with respect to our RSUs:

	Number of Shares	Weighted- Average Grant Date Fair Value per Share
	(In thousands)	
Balance of RSUs outstanding at June 30, 2021	918	\$ 4.14
Granted	607	6.72
Vested	(326)	4.16
Forfeited	(49)	4.80
Balance of RSUs outstanding at March 31, 2022	1,150	\$ 5.45

Performance Stock Units (PSUs)

The following table presents a summary of activity during the nine months ended March 31, 2022 with respect to our PSUs:

	Number of Shares (In thousands)
Balance of PSUs outstanding at June 30, 2021	1,084
Granted	575
Vested	(629)
Balance of PSUs outstanding at March 31, 2022	<u>1,030</u>

Employee Stock Purchase Plan (ESPP)

The following table presents a summary of activity during the nine months ended March 31, 2022 under our ESPP:

	Number of Shares (In thousands)
Shares available for issuance at June 30, 2021	250
Shares issued	(64)
Shares available for issuance at March 31, 2022	<u>186</u>

Share-Based Compensation Expense

The following table presents a summary of share-based compensation expense included in each functional line item on our accompanying unaudited condensed consolidated statements of operations:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2022	2021	2022	2021
	(In thousands)			
Cost of revenue	\$ 80	\$ 70	\$ 280	\$ 212
Selling, general and administrative	1,264	803	3,568	1,919
Research and development	268	170	745	405
Total share-based compensation expense	<u>\$ 1,612</u>	<u>\$ 1,043</u>	<u>\$ 4,593</u>	<u>\$ 2,536</u>

The following table presents the remaining unrecognized share-based compensation expense related to our outstanding share-based awards as of March 31, 2022:

	Remaining Unrecognized Compensation Expense (In thousands)	Remaining Weighted- Average Years To Recognize
Stock options	\$ 797	1.8
RSUs	5,468	2.7
PSUs	1,610	1.3
Stock purchase rights under ESPP	71	0.1
	<u>\$ 7,946</u>	

If there are any modifications or cancellations of the underlying unvested share-based awards, we may be required to accelerate, increase or cancel remaining unearned share-based compensation expense. Future share-based compensation expense and unearned share-based compensation will increase to the extent that we grant additional share-based awards.

8. Income Taxes

We utilize the liability method of accounting for income taxes. The following table presents our effective tax rates based upon our provision for income taxes for the periods shown:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2022	2021	2022	2021
Effective tax rate	<u>2%</u>	<u>3%</u>	<u>3%</u>	<u>5%</u>

The difference between our effective tax rates in the periods presented above and the federal statutory rate is primarily due to a tax benefit from our domestic losses being recorded with a full valuation allowance, as well as the effect of foreign earnings taxed at rates differing from the federal statutory rate.

We record net deferred tax assets to the extent we believe it is more likely than not that these assets will be realized. Due to our cumulative losses and uncertainty of generating future taxable income, we have provided a full valuation allowance against our net deferred tax assets as of March 31, 2022 and June 30, 2021.

9. Commitments and Contingencies

From time to time, we are involved in various legal proceedings and claims arising in the ordinary course of our business. Although the results of legal proceedings and claims cannot be predicted with certainty, we currently believe that the final outcome of these ordinary course matters will not, individually or in the aggregate, have a material adverse effect on our business, operating results, financial condition or cash flows. However, regardless of the outcome, litigation can have an adverse impact on us because of legal costs, diversion of management time and resources, and other factors.

Lease Agreements

California Corporate Headquarters Lease

In November 2021, we entered into a building lease agreement (the “Lease”) pursuant to which we will lease approximately 13,767 square feet of office space for our corporate headquarters in Irvine, California. The Lease is to commence on the date which is the earlier to occur of: (a) the date we take possession of the premises following the completion of certain tenant improvements to the premises, but not earlier than February 1, 2022, or (b) the date we commence our regular business activities on the premises. We currently expect to take possession of the premises, and commence the lease, during our fourth fiscal quarter ending June 30, 2022.

The term of the lease will be 84 months from the commencement date, with an option to extend the lease for one 60-month extension period at a basic rent to be agreed upon by the parties or determined pursuant to the Lease. The initial basic rent payable under the Lease will be \$28,900 per month. The basic rent is subject to customary annual rent increases. The aggregate basic rent payable under the Lease during the 84-month term is \$2,700,000. We are also obligated to pay as additional rent our proportionate share of operating expenses, including property taxes. The Lease required us to deliver to the landlord an irrevocable stand-by letter of credit in the amount of \$50,000 as security in the case of default.

Minnesota Facility Lease

On January 20, 2022, we entered into a lease agreement (the “Lease”) to lease approximately 66,000 square feet in a building in Plymouth, Minnesota (the “Premises”) to house the operations of the TN Companies purchased from CSI in August 2021 and to serve as a central warehouse and shipping hub for all USA-based business of Lantronix.

We took possession of the Premises commencing on the date of the Lease. Beginning on May 1, 2022 (the “Rent Commencement Date”), the initial basic rent payable under the Lease will be \$46,738 per month (with the first three months of rent abated), subject to annualized rent increases of three percent (3%) over the period of the Lease. The initial term of the Lease (the “Initial Term”) commences on the date of the Lease and ends on July 31, 2032. The aggregate basic rent payable under the Lease during the Initial Term is approximately \$6,500,000. We are also obligated to pay as additional rent our proportionate share of operating expenses, including property taxes.

The Lease contains an option to extend the lease for one 60-month extension period at the net rent rate for the last year of the Initial Term or the then-market net rent, as determined pursuant to the Lease, as well as a right of first offer for Lantronix on any space adjacent to the Premises during the Initial Term. We also have the right to terminate the Lease at the end of the 87th full calendar month after the Rent Commencement Date (the “Early Termination Date”) by delivery of a written notice at least six months prior to the Early Termination Date and payment of a termination fee. In addition, the landlord will reimburse Lantronix for its actual out-of-pocket costs for certain tenant improvements to the Premises, with an allowance of up to \$1,500,000 to be paid in three installments in accordance with the Lease.

We have accounted for this lease as an operating lease in accordance with ASC 842. We recorded a right of use asset of \$6,954,000 and lease liability of \$6,954,000 at the inception of the lease based upon a discount rate of 3.9% over a term of 10.5 years.

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 together with our unaudited condensed consolidated financial statements and the related notes included in Part I, Item 1 of this Quarterly Report on Form 10-Q for the three months ended March 31, 2022 (the “Report”). This discussion and analysis contains forward-looking statements that are based on our current expectations and reflect our plans, estimates and anticipated future financial performance. See the section of this Report entitled “Cautionary Note Regarding Forward-Looking Statements” for additional information. These statements involve numerous risks and uncertainties. Our actual results may differ materially from those expressed or implied by these forward-looking statements as a result of many factors, including those set forth in “Risk Factors” in Part II, Item 1A of this Report.

Unless otherwise indicated by the context, all references to the “Company”, “Lantronix”, “we”, “us”, and “our” in this Quarterly Report on Form 10-Q include Lantronix, Inc. and its consolidated subsidiaries.

Overview

Lantronix, Inc. is a global provider of software as a service (“SaaS”), engineering services, and hardware for Edge Computing, the Internet of Things (“IoT”), and Remote Environment Management (“REM”). We enable our customers to provide reliable and secure solutions while accelerating their time to market. Our products and services dramatically simplify operations through the creation, development, deployment, and management of customer projects at scale while providing quality, reliability and security.

We conduct our business globally and manage our sales teams by three geographic regions: the Americas; Europe, Middle East, and Africa (“EMEA”); and Asia Pacific Japan (“APJ”).

Products and Solutions Overview

We organize our products and solutions into three product lines: IoT, REM and Other.

IoT

IoT Connectivity

Our IoT connectivity products typically connect to one or more existing machines or are built into new industrial devices to provide network connectivity. Our products are designed to enhance the value and utility of machines by making the data from the machines available to users, systems and processes or by controlling their properties and features over the network. Our IoT connectivity products may be embedded into new designs or attached to existing machines. These products include wired and wireless connections that enhance the value and utility of modern electronic systems and equipment by providing secure network connectivity, power for IoT end devices through Power over Ethernet (“PoE”), application hosting, protocol conversion, media conversion, secure access for distributed IoT deployments and many other functions.

IoT Compute

Our IoT compute products typically are embedded into a customer product, enabling advanced application functionality at the edge. Our products are designed to deliver advanced functionality and reduce time to market by leveraging our engineering expertise, engineering services, manufacturing experience, and strategic System on Chip (“SoC”) partners. Our compute products are normally embedded into new designs. These products include application processing that delivers compute to meet customer needs for data transformation, computer vision, machine learning, augmented / virtual reality, audio / video aggregation and distribution, and custom applications at the edge. Many of the products are offered with software tools intended to further accelerate our customers’ time-to-market and increase their value add. Most of our IoT compute products are pre-certified in a number of countries thereby significantly reducing our OEM customers’ regulatory certification costs and accelerating their time to market.

IoT Telematics

Our IoT telematics products are typically integrated into an OEM's or System Integrator's ("SI") products. Our smart tracking devices are designed to deliver robust data logging and positional tracking functionality and reliability for supply chain and logistics solutions. Our telematics devices are designed to be flexible in the field and offer a variety of connectivity options to suit the customers' needs across 2G, 3G, 4G, and LTE cellular networks. These power efficient products are designed to support communications across interfaces and industrial protocols for vehicle, fleet, and asset tracking and management. Many of the products are offered with software tools intended to further accelerate our customers' time-to-market and increase their value add. Most of our IoT Telematics products are pre-certified in a number of countries thereby significantly reducing our OEM customers' regulatory certification costs and accelerating their time to market.

Engineering Services

We leverage our engineering expertise and product development best practices to deliver high quality, innovative products, cost-effectively and on time.

Our engineering services flexible business model allows for choosing turnkey product development or team augmentation for accelerating complex areas of product development such as; camera development and tuning, voice control, machine learning, artificial intelligence, computer vision, augmented / virtual reality, mechanical and radio-frequency design, thermal and power optimization, or in any specific area a customer needs assistance.

In addition to our production-ready edge computing solutions, we offer experienced multidisciplinary engineering services across complete aspects of IoT product development, including hardware engineering, software engineering, mechanical engineering, rapid prototyping, and quality assurance.

Software as a Service

Our SaaS platform provides single pane of glass management for IoT deployments. Our platform enables customers to easily deploy, monitor, manage, and automate across their global deployments, all from a single platform login. OEMs and SIs can leverage our platform multitenancy functionality for supporting a wide customer base while ensuring customer separation. Over the Air ("OTA") updates make it easy to ensure the latest security patches, firmware, and configurations are deployed and functional.

REM

Today, organizations are managing an ever-increasing number of devices and data on enterprise networks where 24/7 reliability is mission critical. REM allows for full comprehension and control of an IT deployment, across a range of sensors data (temperature, humidity, light, acceleration, open / close, etc.) providing status and alerting, automation, and remote control of devices and end stations. REM designs may be part of an out of band ("OOB") or in band network design. OOB is a technique that uses a dedicated management network to access critical infrastructure components to ensure production independent management connectivity. REM allows organizations to effectively monitor, manage, and control their enterprise IT equipment and facilities (environments), either in or out of band, optimizing their IT support resources.

Our SaaS platform provides single pane of glass management for REM (and IoT) deployments. Our platform enables customers to easily deploy, monitor, manage, and automate across their global deployments, all from a single platform login, virtually connected as though directly on each device. Our platform eliminates the need to have 24/7 personnel on site, and makes it easy to see and drill into an issue quickly, even in large scale deployments.

Our REM product line includes out-of-band management, console management, power management, and IP connected keyboard-video-mouse (commonly referred to as "IPKVM") products that provide remote access to IT and networking infrastructure deployed in test labs, data centers, branch offices, remote sites, and server rooms.

Other

We categorize products that are non-focus or end-of-life as Other.

Recent Developments

Acquisition

On August 2, 2021 we acquired the Transition Networks and Net2Edge businesses (the “TN Companies”) from Communication Systems, Inc. (“CSI”) for an aggregate purchase price of approximately \$30,651,000, which includes earnout payments of up to \$7,000,000 depending on the achievement of certain revenue targets for the TN Companies. The TN Companies provide us with complementary IoT connectivity products and capabilities, including switching, PoE and media conversion and adapter products. In connection with the closing of the acquisition, we entered into new loan agreements with Silicon Valley Bank (“SVB”) which included (i) a new term loan of \$17,500,000 with an available revolving credit facility of up to \$2,500,000 and (ii) a second term loan of \$12,000,000. In January 2022, we fully repaid the \$12,000,000 second term loan.

Refer to Notes 3 and 6 of Notes to Unaudited Condensed Consolidated Financial Statements included in Part I, Item 1 of this Report, which are incorporated herein by reference, for additional discussions regarding the August 2021 acquisition of the TN Companies and related financing arrangements, respectively.

Underwritten Offering

On November 18, 2021, we entered into an underwriting agreement (the “Underwriting Agreement”) with TL Investment GmbH (“TL Investment”) and Canaccord Genuity LLC, as representative of the several underwriters named therein (together, the “Underwriters”), relating to the Company’s offer and sale of 4,700,000 shares (the “Firm Shares”) of our common stock at an initial price to the public of \$7.50 per share. In addition, TL Investment granted the Underwriters a 30-day option to purchase up to an additional 705,000 shares (the “Option Shares”) of our common stock held by TL Investment at the public offering price, less the underwriting discounts. On November 18, 2021, the Underwriters exercised their option to purchase the Option Shares from TL Investment in full. On November 22, 2021, we issued and delivered the Firm Shares and TL Investment delivered the Option Shares.

Net proceeds to Lantronix from the offering of the Firm Shares, after deducting the underwriting discount and offering expenses, were approximately \$32,600,000.

COVID-19 Update

Since the outbreak of the COVID-19 pandemic, we have taken measures to protect the health and safety of our employees and comply with applicable local directives. Most of our employees transitioned to remote working arrangements commencing in March 2020, and many continue to primarily work remotely as of the date hereof. We continue to monitor the implications of the COVID-19 pandemic on our business, as well as our customers’ and suppliers’ businesses, including the emergence of new strains of the virus, current or future government-imposed shutdowns, and the impact of ongoing vaccination efforts.

Our efforts to support customer engagement through industry events, trade shows and business travel also continue to be adversely affected. Prolonged shutdowns, or additional future shutdowns and other restrictions instituted by federal, state and local governments, may lead to a reduction in revenue during the coming quarters. To mitigate potential revenue declines, we continue to adjust our go-to-market approach by adding more distributors and value-added resellers, who are closer to the customers and end-customers.

Our supply chain still faces challenges, as most of our manufacturing is performed in Thailand, Taiwan and China. We have experienced an increase in costs of components for certain products as well as increased freight and logistics costs and we expect these cost increases to continue. These and other factors have contributed to recent delays in shipments to some customers.

Overall, in light of the changing nature and continuing uncertainty around the COVID-19 pandemic, including the emergence of new, highly-contagious variants, our ability to predict the impact of the COVID-19 pandemic on our business in future periods remains limited. The full effects of the pandemic on our business are unlikely to be fully realized, or reflected in our financial results, until future periods.

Recent Accounting Pronouncements

Refer to *Note 1* of Notes to Unaudited Condensed Consolidated Financial Statements, included in Part I, Item 1 of this Report, which is incorporated herein by reference, for a discussion of recent accounting pronouncements.

Critical Accounting Policies and Estimates

The accounting policies that have the greatest impact on our financial condition and results of operations and that require the most judgment are those relating to revenue recognition, allowance for doubtful accounts, inventory valuation, warranty reserves, restructuring charges, valuation of deferred income taxes, business combinations, goodwill and intangible assets and stock-based compensation. These policies are described in further detail in our Annual Report on Form 10-K for the year ended June 30, 2021 and filed with the Securities and Exchange Commission (the “SEC”) on August 27, 2021 (the “Form 10-K”) and have not changed significantly during the nine months ended March 31, 2022 as compared to what was previously disclosed in the Form 10-K.

Results of Operations – Three Months Ended March 31, 2022 Compared to the Three Months Ended March 31, 2021

Summary

In the three months ended March 31, 2022, our net revenue increased by \$15,216,000 or 88.9%, compared to the three months ended March 31, 2021. The increase in net revenue was driven by a 109.3% increase in net revenue in our IoT product line, as well as a 9.3% increase in net revenue in our REM product line. We had a net loss of \$3,190,000 for the three months ended March 31, 2022 compared to a net loss of \$1,187,000 for the three months ended March 31, 2021. The increase in net loss was primarily driven by an increase in costs directly related to the acquisition of the TN Companies, including increased amortization of purchased intangible assets, as well as the charge recorded to remeasure the fair value of earnout consideration.

Net Revenue

The following tables present our net revenue by product line and by geographic region:

	Three Months Ended March 31,				Change	
	2022	% of Net Revenue	2021	% of Net Revenue	\$	%
(In thousands, except percentages)						
IoT	\$ 28,587	88.4%	\$ 13,661	79.9%	\$ 14,926	109.3%
REM	3,614	11.2%	3,305	19.3%	309	9.3%
Other	123	0.4%	142	0.8%	(19)	(13.4%)
	<u>\$ 32,324</u>	<u>100.0%</u>	<u>\$ 17,108</u>	<u>100.0%</u>	<u>\$ 15,216</u>	<u>88.9%</u>

	Three Months Ended March 31,				Change	
	2022	% of Net Revenue	2021	% of Net Revenue	\$	%
(In thousands, except percentages)						
Americas	\$ 20,448	63.3%	\$ 8,615	50.4%	\$ 11,833	137.4%
EMEA	5,071	15.7%	4,096	23.9%	975	23.8%
APJ	6,805	21.0%	4,397	25.7%	2,408	54.8%
	<u>\$ 32,324</u>	<u>100.0%</u>	<u>\$ 17,108</u>	<u>100.0%</u>	<u>\$ 15,216</u>	<u>88.9%</u>

IoT

Net revenue from our IoT product line for the three months ended March 31, 2022 increased compared to the three months ended March 31, 2021 primarily due to the contribution of product sales from the acquisition of the TN Companies, mostly in the Americas region, which contributed approximately 30% of our total net revenues for the three months ended March 31, 2022. We also experienced organic growth in our pre-acquisition business driven by our SoC products and related engineering services, and xPico and XPort, across all regions.

REM

Net revenue from our REM product line for the three months ended March 31, 2022 increased compared to the three months ended March 31, 2021 due primarily to increased unit sales of our SLS product family in the Americas.

Other

Net revenue from our Other products, which are comprised of non-focus and end-of-life product families, decreased slightly in the EMEA and APJ regions.

Gross Profit

Gross profit represents net revenue less cost of revenue. Cost of revenue consists primarily of the cost of raw material components, subcontract labor assembly from contract manufacturers, direct and indirect personnel expenses related to professional services, manufacturing overhead, inventory reserves for excess and obsolete products or raw materials, warranty costs, royalties and share-based compensation.

The following table presents our gross profit:

	Three Months Ended March 31,				Change	
	2022	% of Net Revenue	2021	% of Net Revenue	\$	%
(In thousands, except percentages)						
Gross profit	\$ 13,616	42.1%	\$ 7,718	45.1%	\$ 5,898	76.4%

Gross profit as a percent of revenue (referred to as “gross margin”) for the three months ended March 31, 2022 decreased compared to the three months ended March 31, 2021 due primarily to higher supply chain and logistics costs. The decrease in gross margin is also the result of sales mix, whereby we experienced growth in unit sales of our SoC products and also growth in our engineering services revenues, both of which typically carry lower gross margins than some of our other legacy product families.

Selling, General and Administrative

Selling, general and administrative expenses consist of personnel-related expenses, including salaries and commissions, share-based compensation, facility expenses, information technology, trade show expenses, advertising, and legal and accounting fees.

The following table presents our selling, general and administrative expenses:

	Three Months Ended March 31,				Change	
	2022	% of Net Revenue	2021	% of Net Revenue	\$	%
(In thousands, except percentages)						
Personnel-related expenses	\$ 4,375		\$ 2,948		\$ 1,427	48.4%
Professional fees and outside services	1,325		628		697	111.0%
Advertising and marketing	605		242		363	150.0%
Facilities and insurance	467		330		137	41.5%
Share-based compensation	1,264		803		461	57.4%
Other	290		44		246	559.1%
Selling, general and administrative	\$ 8,326	25.8%	\$ 4,995	29.2%	\$ 3,331	66.7%

Selling, general and administrative expenses for the three months ended March 31, 2022 increased when compared to the three months ended March 31, 2021 primarily due to (i) higher personnel-related expenses as we added headcount from the acquisition of the TN Companies, (ii) increased professional fees and outside services costs for legal and other services, as well as transition services fees paid to CSI related to the acquisition of the TN Companies, (iii) increased share-based compensation expenses due to additional grants of performance stock units and other stock awards with higher fair values compared to the prior year and (iv) higher marketing spending, including on various events and trade shows that were largely halted in the prior year due to the COVID-19 pandemic.

Research and Development

Research and development expenses consist of personnel-related expenses, including share-based compensation, as well as expenditures to third-party vendors for research and development activities and product certification costs. Our quarterly costs related to outside services and product certifications vary from period to period depending on our level of development activities.

The following table presents our research and development expenses:

	Three Months Ended March 31,				Change	
	2022	% of Net Revenue	2021	% of Net Revenue	\$	%
(In thousands, except percentages)						
Personnel-related expenses	\$ 2,791		\$ 1,724		\$ 1,067	61.9%
Facilities	664		365		299	81.9%
Outside services	359		3		356	11866.7%
Product certifications	171		125		46	36.8%
Share-based compensation	268		170		98	57.6%
Other	230		132		98	74.2%
Research and development	\$ 4,483	13.9%	\$ 2,519	14.7%	\$ 1,964	78.0%

Research and development expenses for the three months ended March 31, 2022 increased when compared to the three months ended March 31, 2021 primarily due to (i) an increase in personnel-related costs driven by additions to headcount from both the TN Companies acquisition and internal growth, (ii) higher facility-related costs as we opened our new facility in Germany and expanded our engineering teams and (iii) higher outside services costs primarily related to the timing of product development projects requiring outsourced engineering resources.

Results of Operations – Nine Months Ended March 31, 2022 Compared to the Nine Months Ended March 31, 2021

Summary

In the nine months ended March 31, 2022, our net revenue increased by \$42,871,000 or 84.3%, compared to the nine months ended March 31, 2021. The increase in net revenue was driven by a 91.8% increase in net revenue in our IoT product line, as well as a 51.7% increase in net revenue in our REM product line. We had a net loss of \$7,868,000 for the nine months ended March 31, 2022 compared to a net loss of \$2,948,000 for the nine months ended March 31, 2021. The increase in net loss was primarily driven by an increase in costs directly related to the acquisition of the TN Companies, including increased amortization of purchased intangible assets, as well as the charge recorded to remeasure the fair value of earnout consideration related to such acquisition.

Net Revenue

The following tables present our net revenue by product line and by geographic region:

	Nine Months Ended March 31,				Change	
	2022	% of Net Revenue	2021	% of Net Revenue	\$	%
(In thousands, except percentages)						
IoT	\$ 79,939	85.3%	\$ 41,683	82.0%	\$ 38,256	91.8%
REM	13,357	14.3%	8,802	17.3%	4,555	51.7%
Other	414	0.4%	354	0.7%	60	16.9%
	<u>\$ 93,710</u>	<u>100.0%</u>	<u>\$ 50,839</u>	<u>100.0%</u>	<u>\$ 42,871</u>	<u>84.3%</u>

	Nine Months Ended March 31,				Change	
	2022	% of Net Revenue	2021	% of Net Revenue	\$	%
(In thousands, except percentages)						
Americas	\$ 58,748	62.7%	\$ 27,567	54.2%	\$ 31,181	113.1%
EMEA	15,481	16.5%	11,475	22.6%	4,006	34.9%
APJ	19,481	20.8%	11,797	23.2%	7,684	65.1%
	<u>\$ 93,710</u>	<u>100.0%</u>	<u>\$ 50,839</u>	<u>100.0%</u>	<u>\$ 42,871</u>	<u>84.3%</u>

IoT

Net revenue from our IoT product line for the nine months ended March 31, 2022 increased compared to the nine months ended March 31, 2021 primarily due to the contribution of product sales from the acquisition of the TN Companies, mostly in the Americas region, which contributed slightly over 28% of our total net revenue for the nine months ended March 31, 2022. We also experienced organic growth in our pre-acquisition business driven by (i) our SoC products and related engineering services, (ii) our xPico product family in the Americas and APJ regions and (iii) our UDS family in the Americas region. The overall increase in net revenues was partially offset by a decrease in unit sales in various product families, including (i) SGX in the Americas and EMEA regions and (ii) WiPort in the Americas and APJ regions.

REM

Net revenue from our REM product line for the nine months ended March 31, 2022 increased compared to the nine months ended March 31, 2021 due primarily to increased unit sales of our SLC8000 product family in the Americas, and to a lesser extent, EMEA and APJ.

Other

Net revenue from our Other products, which are comprised of non-focus and end-of-life product families, increased slightly in the EMEA region.

Gross Profit

The following table presents our gross profit:

	Nine Months Ended March 31,				Change	
	2022	% of Net Revenue	2021	% of Net Revenue	\$	%
	(In thousands, except percentages)					
Gross profit	\$ 40,519	43.2%	\$ 22,953	45.1%	\$ 17,566	76.5%

Gross profit as a percent of revenue (referred to as “gross margin”) for the nine months ended March 31, 2022 decreased compared to the nine months ended March 31, 2021 due primarily to our revenue mix. We saw significant growth in unit sales of our SoC products and growth in our engineering services revenues, which typically carry lower gross margins than some of our other legacy product families. Gross margin for the nine months ended March 31, 2022 was also negatively impacted by (i) higher supply chain and logistics costs and (ii) the amortization of unrealized profit in acquired inventory from the TN Companies in the amount of approximately \$380,000. The overall decrease in our gross margins in the current year period was partially offset by growth in unit sales of some of our higher-margin legacy products, along with the margin contribution from the products acquired from the TN Companies.

Selling, General and Administrative

The following table presents our selling, general and administrative expenses:

	Nine Months Ended March 31,				Change	
	2022	% of Net Revenue	2021	% of Net Revenue	\$	%
	(In thousands, except percentages)					
Personnel-related expenses	\$ 14,047		\$ 8,938		\$ 5,109	57.2%
Professional fees and outside services	4,159		1,755		2,404	137.0%
Advertising and marketing	1,477		650		827	127.2%
Facilities and insurance	1,015		1,080		(65)	(6.0%)
Share-based compensation	3,568		1,919		1,649	85.9%
Other	901		405		496	122.5%
Selling, general and administrative	\$ 25,167	26.9%	\$ 14,747	29.0%	\$ 10,420	70.7%

Selling, general and administrative expenses for the nine months ended March 31, 2022 increased when compared to the nine months ended March 31, 2021 primarily due to (i) higher personnel-related expenses as we added headcount from the acquisition of the TN Companies and also recorded higher variable compensation expenses, (ii) increased professional fees and outside services costs for legal and other services, as well as transition services fees paid to the seller for the acquisition of the TN Companies, (iii) increased share-based compensation expense due to additional grants of performance stock units and other stock awards with higher fair values compared to the prior year and (iv) higher marketing spending, including on various events and trade shows that were largely halted in the prior year due to the COVID-19 pandemic.

Research and Development

The following table presents our research and development expenses:

	Nine Months Ended March 31,				Change	
	2022	% of Net Revenue	2021	% of Net Revenue	\$	%
(In thousands, except percentages)						
Personnel-related expenses	\$ 8,322		\$ 5,310		\$ 3,012	56.7%
Facilities	1,735		934		801	85.8%
Outside services	793		138		655	474.6%
Product certifications	546		358		188	52.5%
Share-based compensation	745		405		340	84.0%
Other	693		395		298	75.4%
Research and development	<u>\$ 12,834</u>	<u>13.7%</u>	<u>\$ 7,540</u>	<u>14.8%</u>	<u>\$ 5,294</u>	<u>70.2%</u>

Research and development expenses for the nine months ended March 31, 2022 increased when compared to the nine months ended March 31, 2021 primarily due to (i) an increase in personnel-related costs driven by additions to headcount from both the TN Companies acquisition and internal growth, (ii) higher facility-related costs as we opened our new facility in Germany and expanded our engineering teams, (iii) increased outside services costs primarily related to the timing of product development projects requiring outsourced engineering resources, and (iv) increased share-based compensation expense due to additional grants of performance stock units and other stock awards with higher fair values compared to the prior year.

Restructuring, Severance and Related Charges

During the nine months ended March 31, 2022, we incurred charges of approximately \$760,000 related to headcount reductions and restructuring of certain non-essential operations, mostly related to cost savings and synergies to be gained from the acquisition of the TN Companies.

We may incur additional restructuring, severance and related charges in future periods as we continue to identify cost savings and synergies related to our acquisitions and general business operations.

Acquisition-Related Costs

During the nine months ended March 31, 2022, we incurred approximately \$763,000 of costs primarily in connection with the acquisition of the TN Companies. These costs were mainly comprised of banking, legal and other professional fees.

Interest Income (Expense), Net

For the nine months ended March 31, 2022, we incurred net interest expense due to borrowings on our credit facilities. We also earn interest income on our domestic cash balance.

Loss on Extinguishment of Debt

For the nine months ended March 31, 2022, we recognized a non-cash loss on the extinguishment of our mezzanine term loan facility of \$764,000, representing the write-off of unamortized deferred financing costs.

Other Income (Expense), Net

Our other income (expense), net, is comprised primarily of foreign currency remeasurement and transaction adjustments related to our foreign subsidiaries whose functional currency is the U.S. dollar.

Provision for Income Taxes

Refer to *Note 8* of Notes to Unaudited Condensed Consolidated Financial Statements, included in Part I, Item 1 of this Report, which is incorporated herein by reference, for a discussion regarding our provision for income taxes.

Liquidity and Capital Resources

Liquidity

The following table presents details of our working capital and cash and cash equivalents:

	March 31, 2022	June 30, 2021 (In thousands)	Change
Working capital	\$ 51,821	\$ 20,289	\$ 31,532
Cash and cash equivalents	\$ 22,782	\$ 9,739	\$ 13,043

In November 2021, we sold 4,700,000 shares of our common stock in an underwritten public offering. We received net cash proceeds from the offering of approximately \$32,600,000. Refer to *Note 7* of Notes to Unaudited Condensed Consolidated Financial Statements, included in Part I, Item 1 of this Report for additional information.

In January 2022, we terminated our \$12,000,000 mezzanine term loan facility that was originated in August 2021. In connection with this termination, we paid a total of \$12,152,500 to pay off the facility in full.

In February 2022, we entered into an amendment to our Senior Credit Facilities (as defined in *Note 6* of Notes to Unaudited Condensed Consolidated Financial Statements, included in Part I, Item 1 of this Report) which (i) increased the amount available under the revolving credit facility from \$2,500,000 to \$7,500,000, (ii) removed and replaced LIBOR benchmark provisions with Term SOFR benchmark provisions and (iii) provided that advances under the Senior Credit Facilities bear interest at Term SOFR or the Prime Rate, at the option of Lantronix, plus a margin that ranges from 3.10% to 4.10% in the case of Term SOFR and 1.50% to 2.50% in the case of the Prime Rate, depending on our total leverage with a Term SOFR floor of 0.00% and a Prime Rate floor of 3.25%. We paid a nonrefundable fee of \$25,000 in connection with this amendment to our Senior Credit Facilities.

Our principal sources of cash and liquidity include our existing cash and cash equivalents, borrowings and amounts available under our loan agreement with our bank, and cash generated from operations. We believe that these sources will be sufficient to fund our current requirements for working capital, capital expenditures and other financial commitments for at least the next 12 months. We anticipate that the primary factors affecting our cash and liquidity are net revenue, working capital requirements and capital expenditures.

Management defines cash and cash equivalents as highly liquid deposits with original maturities of 90 days or less when purchased. We maintain cash and cash equivalents balances at certain financial institutions in excess of amounts insured by federal agencies. Management does not believe this concentration subjects us to any unusual financial risk beyond the normal risk associated with commercial banking relationships. We frequently monitor the third-party depository institutions that hold our cash and cash equivalents. Our emphasis is primarily on safety of principal and secondarily on maximizing yield on those funds.

Our future working capital requirements will depend on many factors, including the following: timing and amount of our net revenue; our product mix and the resulting gross margins; research and development expenses; selling, general and administrative expenses; and expenses associated with any strategic partnerships, acquisitions or infrastructure investments.

From time to time, we may seek additional capital from public or private offerings of our capital stock, borrowings under our existing or future credit lines or other sources in order to (i) develop or enhance our products, (ii) take advantage of strategic opportunities, (iii) respond to competition or (iv) continue to operate our business. We currently have a Form S-3 shelf registration statement on file with the SEC. If we issue equity securities to raise additional funds, our existing stockholders may experience dilution, and the new equity securities may have rights, preferences and privileges senior to those of our existing stockholders. If we issue debt securities to raise additional funds, we may incur debt service obligations, become subject to additional restrictions that limit or restrict our ability to operate our business, or be required to further encumber our assets. There can be no assurance that we will be able to raise any such capital on terms acceptable to us, if at all.

COVID-19 Update

We have not experienced any significant payment delays or defaults by our customers as a result of the COVID-19 pandemic. However, additional economic shutdowns or a prolonged economic recovery may lead to declines in billings and cash collections and result in an unfavorable impact on our financial results in future periods. While we do have a credit line available, financial covenants associated with the credit line may not enable us to draw down funds as needed. We have in place a contingency plan that significantly reduces operating costs in the event that we experience liquidity issues in order to help mitigate our liquidity risk.

Bank Loan Agreements

Refer to *Note 6* of Notes to Unaudited Condensed Consolidated Financial Statements, included in Part I, Item 1 of this Report, which is incorporated herein by reference, for a discussion of our loan agreements.

Cash Flows

The following table presents the major components of the unaudited condensed consolidated statements of cash flows:

	Nine Months Ended March 31,		Change
	2022	2021 (In thousands)	
Net cash provided by (used in) operating activities	\$ (6,066)	\$ 2,584	\$ (8,650)
Net cash used in investing activities	(24,767)	(665)	(24,102)
Net cash provided by (used in) financing activities	43,876	(1,333)	45,209

Operating Activities

Cash used in operating activities during the nine months ended March 31, 2022 increased compared to the prior year period as a result of an increase in our net loss, which was mainly driven by an increase in operating expenses. For the nine months ended March 31, 2022, our net loss included \$13,292,000 of non-cash charges, while the changes in operating assets and liabilities used net cash of \$11,490,000.

Our net inventories increased by \$18,107,000, or 120.2%, from June 30, 2021 to March 31, 2022. Of this increase, \$7,830,000 of net inventories were acquired in the TN Companies acquisition. The remainder of the increase resulted primarily from a build-up of finished goods and critical long-lead time components as we continue to experience lead time and supply constraints.

Accounts receivable increased by \$9,674,000, or 71.6%, from June 30, 2021 to March 31, 2022, of which \$5,156,000 was acquired in the TN Companies acquisition. The remainder of the increase is primarily due to the increase and timing of our sales and related payments from customers.

Accounts payable increased by \$6,388,000, or 70.0%, from June 30, 2021 to March 31, 2022, of which \$1,872,000 was acquired in the TN Companies acquisition. The remainder of the increase is primarily due to the increase and timing of our inventory purchases and related payments to our vendors.

Investing Activities

Net cash used in investing activities during the nine months ended March 31, 2022 was driven by the acquisition of the TN Companies, which used net cash of \$23,629,000. We also used cash for the purchase of property and equipment, primarily related to various tooling, test and office equipment.

Financing Activities

Net cash provided by financing activities during the nine months ended March 31, 2022 resulted primarily from (i) net proceeds from our public offering of \$32,600,000 and (ii) \$29,500,000 in gross proceeds received from our credit facilities with SVB, partially offset by the repayment of our previous term loan in the amount of \$3,750,000 and the mezzanine credit facility in the amount of \$12,000,000. We also used cash of \$1,646,000 for tax withholdings paid on behalf of employees for restricted shares.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

As a smaller reporting company, we are not required to provide the information required by this Item 3.

Item 4. Controls and Procedures

(a) Evaluation of Disclosure Controls and Procedures

We maintain disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)) that are designed to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is (i) recorded, processed, summarized and reported within the time periods specified in SEC rules and forms and (ii) is accumulated and communicated to our management, including our principal executive officer and principal financial officer, as appropriate, to allow timely decisions regarding required disclosure.

We carried out an evaluation, under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, of the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this Report. Based upon that evaluation, our principal executive officer and principal financial officer concluded that our disclosure controls and procedures were effective as of March 31, 2022 at the reasonable assurance level.

(b) Changes in Internal Control over Financial Reporting

There were no changes in our internal control over financial reporting identified in connection with the evaluation required by Rule 13a-15(f) and 15d-15(f) of the Exchange Act that occurred during the quarter ended March 31, 2022, that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

(c) Inherent Limitation on Effectiveness of Controls

A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of a simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the controls. The design of any system of controls is also based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, controls may become inadequate because of changes in conditions, or the degree of compliance with policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

Refer to Note 9 of Notes to Unaudited Condensed Consolidated Financial Statements, included in Part I, Item 1 of this Report, which is incorporated herein by reference, for a discussion of legal proceedings.

Item 1A. Risk Factors

We operate in a rapidly changing environment that involves numerous risks and uncertainties. Before deciding to purchase, hold or sell our common stock, you should carefully consider the risks described in this section, as well as other information contained in this Report and in our other filings with the SEC. This section should be read in conjunction with the unaudited condensed consolidated financial statements and accompanying notes thereto included in Item 1 of this Report, and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included in Item 2 of this Report. If any of these risks or uncertainties actually occurs, our business, financial condition, results of operations or prospects could be materially harmed. In that event, the market price for our common stock could decline and you could lose all or part of your investment. In addition, risks and uncertainties not presently known to us or that we currently deem immaterial may also adversely affect our business.

The risks and uncertainties discussed below update and supersede the risks and uncertainties previously disclosed in Part I, Item 1A of our Annual Report on Form 10-K for the fiscal year ended June 30, 2021, which was filed with the SEC on August 27, 2021. There have been no material changes to the risks and uncertainties previously disclosed in such Annual Report on Form 10-K.

Risks Related to Our Operations and Industry

The effect of COVID-19 and other possible pandemics and similar outbreaks could result in material adverse effects on our business, financial position, results of operations and cash flows.

The COVID-19 outbreak spread globally and led governments and other authorities around the world, including federal, state and local authorities in the United States and abroad, to impose measures intended to reduce its spread, including restrictions on freedom of movement and business operations such as travel bans, border closings, business limitations and closures (subject to exceptions for essential operations and businesses), quarantines and shelter-in-place orders. Periodic surges of COVID-19, including due to more contagious and/or vaccine-resistant variants, have resulted in the reimposition of certain restrictions and may lead to other restrictions being implemented in response to efforts to reduce the spread of COVID-19. Given the dynamic nature of these circumstances and the related adverse impact these restrictions have had, and may continue to have, on the economy generally, our business and the business of our suppliers, our results of operations and financial condition may be adversely impacted by the COVID-19 pandemic.

Beginning in March 2020, most of our employees transitioned to remote working arrangements, which are continuing through the date of this Report. There can be no assurance that these arrangements will not ultimately result in lower work efficiency and productivity, which in turn may adversely affect our business. In addition, the COVID-19 pandemic resulted in industry events, trade shows and business travel being suspended, cancelled and/or significantly curtailed. The cessation of trade shows and business travel resulted in our lead pipeline being negatively impacted, which negatively affected our sales during the past two years. While most industry events, trade shows and business travel have resumed, if these activities are suspended, cancelled and/or significantly curtailed in the future, whether due to surges of COVID-19 or otherwise related to the pandemic, our sales may continue to be negatively impacted in the future.

In addition, the impact of the COVID-19 pandemic and measures to prevent its spread subject us to various risks and uncertainties that could materially adversely affect our business, results of operations and financial condition, including the following:

- significant volatility or decreases in the demand for our products or extended sales cycles;
- changes in customer behavior and preferences, as customers may experience financial difficulties and/or may delay orders or reduce their spending in light of COVID-19;
- adverse impacts on our ability to distribute or deliver our products or services, including due to the negative impact of COVID-19 on air travel, as well as temporary disruptions, restrictions or closures of the facilities of our suppliers or customers and their contract manufacturers;
- further disruptions in our contract manufacturers’ ability to manufacture our products, as some contract manufacturers and suppliers of materials used in the production of our products are located in areas more severely impacted by COVID-19, which has limited and could further limit our ability to obtain sufficient materials to produce and manufacture our products; and
- volatility in the availability of raw materials and components that our contract manufacturers purchase and volatility in raw material and other input costs.

The duration and extent of the COVID-19 pandemic's effect on our operations and financial condition will depend on future developments, which are highly uncertain and cannot be predicted at this time, including new information which may emerge concerning the severity of COVID-19, actions taken to contain COVID-19, additional surges of COVID-19 infections due to the rate of public acceptance and efficacy of COVID-19 vaccines or due to new and more contagious and/or vaccine resistant variants, and how quickly and to what extent normal economic and operating conditions can resume. Even after the COVID-19 pandemic has subsided, we may experience adverse impacts to our business, financial condition, results of operations, and prospects as a result of its global economic impact, including any economic downturn or recession that has occurred or may occur in the future. The adverse impact of the COVID-19 pandemic on our business, results of operations and financial condition could be material.

We may experience constraints in the supply of certain materials and components that could affect our operating results.

Some of our integrated circuits are only available from a single source and in some cases, are no longer being manufactured. From time to time, integrated circuits, and potentially other components used in our products, will be phased out of production by the manufacturer. When this happens, we attempt to purchase sufficient inventory to meet our needs until a substitute component can be incorporated into our products. Nonetheless, we may be unable to purchase sufficient components to meet our demands, or we may incorrectly forecast our demands, and purchase too many or too few components. In addition, our products use components that have been in the past and may in the future be subject to market shortages and substantial price fluctuations, whether due to the COVID-19 pandemic, the war between Ukraine and Russia or otherwise. From time to time, we have been unable to meet customer orders because we were unable to purchase necessary components for our products. We do not have long-term supply arrangements with most of our vendors to obtain necessary components, including semiconductor chips, or technology for our products and instead purchase components on a purchase order basis. If we are unable to purchase components from these suppliers, our product shipments could be prevented or delayed, which could result in a loss of sales. If we are unable to meet existing orders or to enter into new orders because of a shortage in components, we will likely lose net revenue, risk losing customers and risk harm to our reputation in the marketplace, which could adversely affect our business, financial condition or results of operations. For instance, we have recently experienced increased delays in shipments of semiconductor chips. As a result, we have sought alternate sources of certain components, which have been at a higher cost. Because semiconductor chips continue to be subject to an ongoing significant shortage, our ability to source components that use semiconductor chips has been adversely affected. These supply interruptions have resulted in increased component delivery lead times and increased costs to obtain components with available semiconductor chips. To the extent this semiconductor chip shortage or other shortages continue, the production of our products may be impacted.

Future operating results depend upon our ability to timely obtain components in sufficient quantities and on acceptable terms.

We and our contract manufacturers are responsible for procuring raw materials for our products. Our products incorporate some components and technologies that are only available from single or limited sources of supply. Depending on a limited number of suppliers exposes us to risks, including limited control over pricing, availability, quality and delivery schedules. Moreover, due to our limited sales, we may not be able to convince suppliers to continue to make components available to us unless there is demand for these components from their other customers. If any one or more of our suppliers cease to provide us with sufficient quantities of components in a timely manner or on terms acceptable to us, we would have to seek alternative sources of supply and we may have difficulty identifying additional or replacement suppliers for some of our components.

We outsource substantially all of our manufacturing to contract manufacturers in Asia. If our contract manufacturers are unable or unwilling to manufacture our products at the quality and quantity we request, our business could be harmed.

We use contract manufacturers based in Asia to manufacture substantially all of our products. Generally, we do not have guaranteed supply agreements with our contract manufacturers or suppliers. If any of these subcontractors or suppliers were to cease doing business with us, we might not be able to obtain alternative sources in a timely or cost-effective manner. Our reliance on third-party manufacturers, especially in countries outside of the U.S., exposes us to a number of significant risks, including:

- reduced control over delivery schedules, quality assurance, manufacturing yields and production costs;
- lack of guaranteed production capacity or product supply;
- reliance on these manufacturers to maintain competitive manufacturing technologies;
- unexpected changes in regulatory requirements, taxes, trade laws and tariffs;
- reduced protection for intellectual property rights in some countries;
- differing labor regulations;
- disruptions to the business, financial stability or operations, including due to strikes, labor disputes or other disruptions to the workforce, of these manufacturers;
- compliance with a wide variety of complex regulatory requirements;
- fluctuations in currency exchange rates;
- changes in a country's or region's political or economic conditions;
- effects of terrorist attacks or geopolitical conflicts abroad;
- greater difficulty in staffing and managing foreign operations; and
- increased financial accounting and reporting burdens and complexities.

Any problems that we may encounter with the delivery, quality or cost of our products from our contract manufacturers or suppliers could cause us to lose net revenue, damage our customer relationships and harm our reputation in the marketplace, each of which could materially and adversely affect our business, financial condition or results of operations.

From time to time, we may transition the manufacturing of certain products from one contract manufacturer to another. When we do this, we may incur substantial expenses, risk material delays or encounter other unexpected issues.

Certain of our products are sold into mature markets, which could limit our ability to continue to generate revenue from these products. Our ability to sustain and grow our business depends on our ability to develop, market, and sell new products.

Certain of our products are sold into mature markets that are characterized by a trend of declining demand. As the overall market for these products decreases due to the adoption of new technologies, we expect that our revenues from these products will continue to decline. As a result, our future prospects will depend on our ability to develop and successfully market new products that address new and growing markets. Our failure to develop new products or failure to achieve widespread customer acceptance of any new products could cause us to lose market share and cause our revenues to decline. There can be no assurance that we will not experience difficulties that could delay or prevent the successful development, introduction, marketing and sale of new products or product enhancements. Factors that could cause delays include regulatory and/or industry approvals, product design cycle and failure to identify products or features that customers demand. In addition, the introduction and sale of new products often involves a significant technical evaluation, and we often face delays because of our customers' internal procedures for evaluating, approving and deploying new technologies. For these and other reasons, the sales cycle associated with new products is typically lengthy, often lasting six to 24 months and sometimes longer. Therefore, there can be no assurance that our introduction or announcement of new product offerings will achieve any significant or sustainable degree of market acceptance or result in increased revenue in the near term.

Our software offerings are subject to risks that differ from those facing our hardware products.

We continue to dedicate significant engineering resources to our management software platform, applications, and SaaS offerings, including ConsoleFlow™. These product and service offerings are subject to significant additional risks that are not necessarily related to our hardware products. Our ability to succeed with these offerings will depend in large part on our ability to provide customers with software products and services that offer features and functionality that address the needs of particular businesses. We may face challenges and delays in the development of this product line as the marketplace for products and services evolves to meet the needs and desires of customers. We cannot provide assurances that we will be successful in operating and growing this product line.

In light of these risks and uncertainties, we may not be able to establish or maintain market share for our software and SaaS offerings. As we develop new product lines, we must adapt to market conditions that are unfamiliar to us, such as competitors and distribution channels that are different from those we have known in the past. We have and will encounter competition from other solutions providers, many of whom may have more significant resources than us with which to compete. There can be no assurance that we will recover our investments in this product line, that we will receive meaningful revenue from or realize a profit from this new product line or that diverting our management's attention to this product line will not have a material adverse effect on our existing business, and in turn on our results of operations, financial condition and prospects.

We may experience significant fluctuation in our revenue because the timing of large orders placed by some of our customers is often project-based.

Our operating results fluctuate because we often receive large orders from customers that coincide with the timing of the customer's project. Sales of our products and services may be delayed if customers delay approval or commencement of projects due to budgetary constraints, internal acceptance review procedures, timing of budget cycles or timing of competitive evaluation processes. In addition, sometimes our customers make significant one-time hardware purchases for projects which are not repeated. We sell primarily on a purchase order basis rather than pursuant to long-term contracts, and we expect fluctuations in our revenues as a result of one-time project-based purchases to continue in the future. In addition, our sales may be subject to significant fluctuations based on the acceleration, delay or cancellation of customer projects, or our failure to complete one or a series of significant potential sales. Because a significant portion of our operating expenses are fixed, even a single order can have a disproportionate effect on our quarterly revenues and operating results. As a result of the factors discussed above, and due to the complexities of the industry in which we operate, it is difficult for us to forecast demand for our current or future products with any degree of certainty, which means it is difficult for us to forecast our sales. If our quarterly or annual operating results fall below the expectations of investors or securities analysts, the price of our common stock could decline substantially.

The lengthy sales cycle for our products and services, along with delays in customer completion of projects, make the timing of our revenues difficult to predict.

We have a lengthy sales cycle for many of our products that generally extends between six and 24 months and sometimes longer due to a lengthy customer evaluation and approval process. The length of this process can be affected by factors over which we have little or no control, including the customer's budgetary constraints, timing of the customer's budget cycles, and concerns by the customer about the introduction of new products by us or by our competitors. As a result, sales cycles for customer orders vary substantially among different customers. The lengthy sales cycle is one of the factors that has caused, and may continue to cause, our revenues and operating results to vary significantly from quarter to quarter. In addition, we may incur substantial expenses and devote significant management effort and expense to develop potential relationships that do not result in agreements or revenues, which may prevent us from pursuing other opportunities. Accordingly, excessive delays in sales could be material and adversely affect our business, financial condition or results of operations.

The nature of our products, customer base and sales channels causes us to lack visibility into future demand for our products, which makes it difficult for us to forecast our manufacturing and inventory requirements.

We use forecasts based on anticipated product orders to manage our manufacturing and inventory levels and other aspects of our business. However, several factors contribute to a lack of visibility with respect to future orders, including:

- the lengthy and unpredictable sales cycle for our products that can extend from six to 24 months or longer;
- the project-driven nature of many of our customers' requirements;
- we primarily sell our products indirectly through distributors;
- the uncertainty of the extent and timing of market acceptance of our new products;
- the need to obtain industry certifications or regulatory approval for our products;
- the lack of long-term contracts with our customers;
- the diversity of our product lines and geographic scope of our product distribution;
- we have some customers who make single, non-recurring purchases; and
- a large number of our customers typically purchase in small quantities.

This lack of visibility impacts our ability to forecast our inventory requirements. If we overestimate our customers' future requirements for products, we may have excess inventory, which would increase our costs and potentially require us to write-off inventory that becomes obsolete. Additionally, if we underestimate our customers' future requirements, we may have inadequate inventory, which could interrupt and delay delivery of our products to our customers, harm our reputation, and cause our revenues to decline. If any of these events occur, they could prevent us from achieving or sustaining profitability and the value of our common stock may decline.

Delays in qualifying revisions of existing products for certain of our customers could result in the delay or loss of sales to those customers, which could negatively impact our business and financial results.

Our industry is characterized by intense competition, rapidly evolving technology and continually changing customer preferences and requirements. As a result, we frequently develop and introduce new versions of our existing products, which we refer to as revisions.

Prior to purchasing our products, some of our customers require that products undergo a qualification process, which may involve testing of the products in the customer's system. A subsequent revision to a product's hardware or firmware, changes in the manufacturing process or our selection of a new supplier may require a new qualification process, which may result in delays in sales to customers, loss of sales, or us holding excess or obsolete inventory.

After products are qualified, it can take additional time before the customer commences volume production of components or devices that incorporate our products. If we are unsuccessful or delayed in qualifying any new or revised products with a customer, that failure or delay would preclude or delay sales of these products to the customer, and could negatively impact our financial results. In addition, new revisions to our products could cause our customers to alter the timing of their purchases, by either accelerating or delaying purchases, which could result in fluctuations of our net revenue from quarter to quarter.

We depend on distributors for a majority of our sales and to complete order fulfillment.

We depend on the resale of products through distributor accounts for a substantial majority of our worldwide net revenue. In addition, sales through our top five distributors accounted for approximately 37% of our net revenue in fiscal 2021. A significant reduction of effort by one or more distributors to sell our products or a material change in our relationship with one or more distributors may reduce our access to certain end customers and adversely affect our ability to sell our products. Furthermore, if a key distributor materially defaults on a contract or otherwise fails to perform, our business and financial results would suffer.

In addition, the financial health of our distributors and our continuing relationships with them are important to our success. Our business could be harmed if the financial health of these distributors impairs their performance and we are unable to secure alternate distributors.

Our ability to sustain and grow our business depends in part on the success of our distributors and resellers.

A substantial part of our revenues is generated through sales by distributors and resellers. To the extent they are unsuccessful in selling our products, or if we are unable to obtain and retain a sufficient number of high-quality distributors and resellers, our operating results could be materially and adversely affected. In addition, our distributors and resellers may devote more resources to marketing, selling and supporting products and services that are competitive with ours, than to our products. They also may have incentives to promote our competitors' products over our products, particularly for our competitors with larger volumes of orders, more diverse product offerings and a longer relationship with our distributors and resellers. In these cases, one or more of our important distributors or resellers may stop selling our products completely or may significantly decrease the volume of products they sell on our behalf. This sales structure also could subject us to lawsuits, potential liability and reputational harm if, for example, any of our distributors or resellers misrepresents the functionality of our products or services to customers, violates laws or our corporate policies. If we fail to effectively manage our existing or future distributors and resellers effectively, our business and operating results could be materially and adversely affected.

Changes to the average selling prices of our products could affect our net revenue and gross margins and adversely affect results of operations.

In the past, we have experienced reductions in the average selling prices and gross margins of our products. We expect competition to continue to increase, and we anticipate this could result in additional downward pressure on our pricing. Our average selling prices for our products might also decline as a result of other reasons, including promotional programs introduced by us or our competitors and customers who negotiate price concessions. To the extent we are able to increase prices, we may experience a decline in sales volumes if customers decide to purchase competitive products. If any of these were to occur, our gross margins could decline and we might not be able to reduce the cost to manufacture our products enough or at all to keep up with the decline in prices.

If we are unable to sell our inventory in a timely manner, it could become obsolete, which could require us to write-down or write off obsolete inventory, which could harm our operating results.

At any time, competitive products may be introduced with more attractive features or at lower prices than ours. If this occurs, and for other reasons, we may not be able to accurately forecast demand for our products and our inventory levels may increase. There is a risk that we may be unable to sell our inventory in a timely manner to avoid it becoming obsolete. If we are required to substantially discount our inventory or are unable to sell our inventory in a timely manner, we would be required to increase our inventory reserves or write off obsolete inventory and our operating results could be substantially harmed.

Our failure to compete successfully in our highly competitive market could result in reduced prices and loss of market share.

The market in which we operate is intensely competitive, subject to rapid technological advances and highly sensitive to evolving industry standards. The market can also be affected significantly by new product and technology introductions and marketing and pricing activities of industry participants. Our products compete directly with products produced by a number of our competitors. Many of our competitors and potential competitors have greater financial and human resources for marketing and product development, more experience conducting research and development activities, greater experience obtaining regulatory approval for new products, larger distribution and customer networks, more established relationships with contract manufacturers and suppliers, and more established reputations and name recognition. For these and other reasons, we may not be able to compete successfully against our current or potential future competitors. In addition, the amount of competition we face in the marketplace may change and grow as the market for IoT and M2M networking solutions grows and new companies enter the marketplace. Present and future competitors may be able to identify new markets, adapt new technologies, develop and commercialize products more quickly and gain market acceptance of products with greater success. As a result of these competitive factors, we may fail to meet our business objectives and our business, financial condition and operating results could be materially and adversely affected.

Acquisitions, strategic partnerships, joint ventures or investments may impair our capital and equity resources, divert our management's attention or otherwise negatively impact our operating results.

We may pursue acquisitions, strategic partnerships and joint ventures that we believe would allow us to complement our growth strategy, increase market share in our current markets and expand into adjacent markets, broaden our technology and intellectual property and strengthen our relationships with distributors, OEMs and ODMs. For instance, we acquired Maestro, Intrinsyc and the Transition Networks and Net2Edge businesses of CSI in 2019, 2020 and 2021, respectively. Our previous acquisitions have required, and any future acquisition, partnership, joint venture or investment may also require, that we pay significant cash, issue equity and/or incur substantial debt. Acquisitions, partnerships or joint ventures may also result in the loss of key personnel and the dilution of existing stockholders to the extent we are required to issue equity securities. In addition, acquisitions, partnerships or joint ventures require significant managerial attention, which may be diverted from our other operations. These capital, equity and managerial commitments may impair the operation of our business. Furthermore, acquired businesses may not be effectively integrated, may be unable to maintain key pre-acquisition business relationships, may not result in expected synergies, an increase in revenues or earnings or the delivery of new products, may contribute to increased fixed costs, and may expose us to unanticipated liabilities. If any of these occur, we may fail to meet our business objectives and our business, financial condition and operating results could be materially and adversely affected.

We may experience difficulties associated with utilizing third-party logistics providers.

A majority of our physical inventory management process, as well as the shipping and receiving of our inventory, is performed by third-party logistics providers in Los Angeles, California and Hong Kong. There is a possibility that these third-party logistics providers will not perform as expected and we could experience delays in our ability to ship, receive, and process the related data in a timely manner. This could adversely affect our financial position, results of operations, cash flows and the market price of our common stock.

Relying on third-party logistics providers could increase the risk of the following: failing to receive accurate and timely inventory data, theft or poor physical security of our inventory, inventory damage, ineffective internal controls over inventory processes or other similar business risks out of our immediate control.

Risks Related to Technology, Cybersecurity and Intellectual Property

Cybersecurity breaches and other disruptions could compromise our information and expose us to liability, which could cause our business and reputation to suffer.

In the ordinary course of our business, we collect and store sensitive data, including intellectual property, our proprietary business information and that of our customers, suppliers and business partners, and personally identifiable information of our employees, on our networks and third-party cloud software providers. Increased global information technology ("IT") security threats and more sophisticated and targeted computer crime pose a risk to the security of our systems and networks and the confidentiality, availability and integrity of our data. There have been several recent, highly publicized cases in which organizations of various types and sizes have reported the unauthorized disclosure of customer or other confidential information, as well as cyberattacks involving the dissemination, theft and destruction of corporate information, intellectual property, cash or other valuable assets. There have also been several highly publicized cases in which hackers have requested "ransom" payments in exchange for not disclosing customer or other confidential information or for not disabling the target company's computer or other systems. The secure processing, maintenance and transmission of the information that we collect and store on our systems is critical to our operations and implementing security measures designed to prevent, detect, mitigate or correct these or other IT security threats involves significant costs. Although we have taken steps to protect the security of our information systems, we have, from time to time, experienced threats to our data and systems, including malware, phishing and computer virus attacks, and it is possible that in the future our safety and security measures will not prevent the systems' improper functioning or damage, or the improper access or disclosure of personally identifiable information such as in the event of cyber-attacks. In addition, due to the fast pace and unpredictability of cyber threats, long-term implementation plans designed to address cybersecurity risks become obsolete quickly and, in some cases, it may be difficult to anticipate or immediately detect such incidents and the damage they cause. Any unauthorized access, disclosure or other loss of information could result in legal claims or proceedings, disrupt our operations, damage our reputation, and cause a loss of confidence in our products and services, which could adversely affect our business.

If our products become subject to cybersecurity breaches, or if public perception is that they are vulnerable to cyberattacks, our reputation and business could suffer.

We could be subject to liability or our reputation could be harmed if technologies integrated into our products, or our products, fail to prevent cyberattacks, or if our partners or customers fail to safeguard the systems with security policies that conform to industry best practices. In addition, any cyberattack or security breach that affects a competitor's products could lead to the negative perception that our solutions are or could be subject to similar attacks or breaches.

Some of our software offerings may be subject to various cybersecurity risks, which are particularly acute in the cloud-based technologies operated by us and other third parties that form a part of our solutions.

In connection with certain implementations of our management software platform, application, and SaaS offering, ConsoleFlow, we expect to store, convey and potentially process data produced by devices. This data may include confidential or proprietary information, intellectual property or personally identifiable information of our customers or other third parties with whom they do business. It is important for us to maintain solutions and related infrastructure that are perceived by our customers and other parties with whom we do business to provide a reasonable level of reliability and security. Despite available security measures and other precautions, the infrastructure and transmission methods used by our products and services may be vulnerable to interception, attack or other disruptive problems.

If a cyberattack or other security incident were to allow unauthorized access to or modification of our customers' data or our own data, whether due to a failure with our systems or related systems operated by third parties, we could suffer damage to our brand and reputation. The costs we would incur to address and fix these incidents could significantly increase our expenses. These types of security incidents could also lead to lawsuits, regulatory investigations and increased legal liability, including in some cases contractual costs related to customer notification and fraud monitoring. Further, as regulatory focus on privacy and data security issues continues to increase and worldwide laws and regulations concerning the protection of information become more complex, the potential risks and costs of compliance to our business will intensify.

If software that we incorporate into our products were to become unavailable or no longer available on commercially reasonable terms, it could adversely affect sales of our products, which could disrupt our business and harm our financial results.

Certain of our products contain software developed and maintained by third-party software vendors or which are available through the "open source" software community. We also expect that we may incorporate software from third-party vendors and open source software in our future products. Our business would be disrupted if this software, or functional equivalents of this software, were either no longer available to us or no longer offered to us on commercially reasonable terms. In either case, we would be required to either redesign our products to function with alternate third-party software or open source software, or develop these components ourselves, which would result in increased costs and could result in delays in our product shipments. Furthermore, we might be forced to limit the features available in our current or future product offerings.

Our products may contain undetected software or hardware errors or defects that could lead to an increase in our costs, reduce our net revenue or damage our reputation.

We currently offer warranties ranging from one to five years on each of our products. Our products could contain undetected software or hardware errors or defects. If there is a product failure, we might have to replace all affected products, or we might have to refund the purchase price for the units. Regardless of the amount of testing we undertake, some errors might be discovered only after a product has been installed and used by customers. Any errors discovered after commercial release could result in financial losses and claims against us. Significant product warranty claims against us could harm our business, reputation and financial results and cause the market price of our common stock to decline.

We may not be able to adequately protect or enforce our intellectual property rights, which could harm our competitive position or require us to incur significant expenses to enforce our rights.

We rely primarily on a combination of laws, such as patent, copyright, trademark and trade secret laws, and contractual restrictions, such as confidentiality agreements and licenses, to establish and protect our proprietary rights. Despite any precautions that we have taken:

- laws and contractual restrictions might not be sufficient to prevent misappropriation of our technology or deter others from developing similar technologies;
- other companies might claim intellectual property rights based upon prior use that negatively impacts our ability to enforce our trademarks and patents; and
- policing unauthorized use of our patented technology and trademarks is difficult, expensive and time-consuming, and we might be unable to determine the extent of this unauthorized use.

Also, the laws of some of the countries in which we market and manufacture our products offer little or no effective protection of our proprietary technology. Reverse engineering, unauthorized copying or other misappropriation of our proprietary technology could enable third parties to benefit from our technology without paying us for it. Consequently, we may be unable to prevent our proprietary technology from being exploited by others in the U.S. or abroad, which could require costly efforts to protect our technology. Policing the unauthorized use of our technology, trademarks and other proprietary rights is expensive, difficult and, in some cases, impracticable. Litigation may be necessary in the future to enforce or defend our intellectual property rights, to protect our trade secrets or to determine the validity and scope of the proprietary rights of others. Such litigation could result in substantial costs and diversion of management resources, either of which could harm our business. Accordingly, despite our efforts, we may not be able to prevent third parties from infringing upon or misappropriating our intellectual property, which may harm our business, financial condition and results of operations.

The impact of natural disasters and other business interruptions could negatively impact our supply chain and customers resulting in an adverse impact to our revenues and profitability.

Certain of our components and other materials used in producing our products are from regions susceptible to natural disasters. A natural disaster could damage equipment and inventory at our suppliers' facilities, adversely affecting our supply chain. If we are unable to obtain these materials, we could experience a disruption to our supply chain that would hinder our ability to produce our products in a timely manner, or cause us to seek other sources of supply, which may be more costly or which we may not be able to procure on a timely basis. In addition, our customers may not follow their normal purchasing patterns or temporarily cease purchasing from us due to impacts to their businesses in the region, creating unexpected fluctuations or decreases in our revenues and profitability. Natural disasters in other parts of the world on which our operations are reliant also could have material adverse impacts on our business.

In addition, our operations and those of our suppliers are vulnerable to interruption by fire, earthquake, power loss, telecommunications failure, cybersecurity breaches, IT systems failure, terrorist attacks and other events beyond our control. A substantial portion of our facilities, including our corporate headquarters and other critical business operations, are located near major earthquake faults and, therefore, may be more susceptible to damage if an earthquake occurs. We do not carry earthquake insurance for direct earthquake-related losses. If a business interruption occurs, whether due to a natural disaster or otherwise, our business could be materially and adversely affected.

Risk Related to Liquidity and Capital Resources

We have a history of losses.

We have historically incurred net losses. There can be no assurance that we will generate net profits in future periods. Further, there can be no assurance that we will be cash flow positive in future periods. In the event that we fail to achieve profitability in future periods, the value of our common stock may decline. In addition, if we are unable to achieve or maintain positive cash flows, we would be required to seek additional funding, which may not be available on favorable terms, if at all.

We may need additional capital and it may not be available on acceptable terms, or at all.

To remain competitive, we must continue to make significant investments to operate our business and develop our products. Our future capital requirements will depend on many factors, including the timing and amount of our net revenue, research and development expenditures, expenses associated with any strategic partnerships or acquisitions and infrastructure investments, and expenses related to litigation, each of which could negatively affect our ability to generate additional cash from operations. If cash generated from operations is insufficient to satisfy our working capital requirements, we may need to raise additional capital. Looking ahead at long-term needs, we may need to raise additional funds for a number of purposes, including, but not limited to:

- to fund working capital requirements;
- to update, enhance or expand the range of products we offer;
- to refinance existing indebtedness;
- to increase our sales and marketing activities; or
- to respond to competitive pressures or perceived opportunities, such as investment, acquisition and international expansion activities.

We may seek additional capital from public or private offerings of our capital stock, borrowings under our existing or future credit lines or other sources. If we issue equity or debt securities to raise additional funds, our existing stockholders may experience dilution, and the new equity or debt securities may have rights, preferences and privileges senior to those of our existing stockholders. In addition, if we raise additional funds through collaborations, licensing, joint ventures, or other similar arrangements, it may be necessary to relinquish valuable rights to our potential future products or proprietary technologies, or grant licenses on terms that are not favorable to us. There can be no assurance that we will be able to raise any needed capital on terms acceptable to us, if at all. If we are unable to secure additional financing in sufficient amounts or on favorable terms, we may not be able to develop or enhance our products, take advantage of future opportunities, respond to competition or continue to operate our business.

The terms of our Senior Credit Facilities may restrict our financial and operational flexibility and, in certain cases, our ability to operate.

The terms of our Senior Credit Facilities restrict, among other things, our ability to incur liens, incur indebtedness, dispose of assets, make investments, make certain restricted payments, merge or consolidate and enter into certain speculative hedging arrangements. Further, we are currently and may in the future be required to maintain specified financial ratios, including pursuant to a maximum leverage ratio, a minimum fixed charge coverage ratio or a minimum liquidity test. Our ability to meet those financial ratios and tests can be affected by events beyond our control, and there can be no assurance that we will meet those tests. Pursuant to our amended credit agreement and the related loan and security agreement, we have pledged substantially all of our assets to our senior lender, SVB, and our junior lender, SVB Innovation Credit Fund VIII, L.P.

Risks Related to International Operations

Rising concern regarding international tariffs could materially and adversely affect our business and results of operations.

The current political landscape has introduced significant uncertainty with respect to future trade regulations and existing international trade agreements, as shown by the U.S.-initiated renegotiation of the North America Free Trade Agreement, Brexit in Europe, and the current war between Ukraine and Russia. This uncertainty includes the possibility of imposing tariffs or penalties on products manufactured outside the U.S., including the US government's institution of a 25% tariff on a range of products from China and subsequent tariffs imposed by the U.S. as well as tariffs imposed by trading partners on U.S. goods, the potential for increased trade barriers between the U.K. and the European Union, and export controls or other retaliatory actions against, or restrictions on doing business with Russia, as well as any resulting disruption, instability or volatility in the global markets and industries resulting from such conflict. The institution of trade tariffs both globally and between the U.S. and China specifically, carries the risk of negatively affecting the overall economic conditions of both China and the U.S., which could have a negative impact on us.

We cannot predict whether, and to what extent, there may be changes to international trade agreements or whether quotas, duties, tariffs, exchange controls or other restrictions on our products will be changed or imposed. If we are unable to source our products from the countries where we wish to purchase them, either because of regulatory changes or for any other reason, or if the cost of doing so increases, it could have a material adverse effect on our business, financial condition and results of operations. Furthermore, imposition of tariffs may result in local sourcing initiatives, or other developments that make it more difficult to sell our products in foreign countries, which would negatively impact our business and operating results.

We face risks associated with our international operations that could impair our ability to grow our revenues abroad as well as our overall financial condition.

We believe that our future growth is dependent in part upon our ability to increase sales in international markets. These sales are subject to a variety of risks, including geopolitical events, fluctuations in currency exchange rates, tariffs, import restrictions and other trade barriers, unexpected changes in regulatory requirements, longer accounts receivable payment cycles, potentially adverse tax consequences, and export license requirements. In addition, we are subject to the risks inherent in conducting business internationally, including political and economic instability and unexpected changes in diplomatic and trade relationships. In many markets where we operate, business and cultural norms are different than those in the U.S., and practices that may violate laws and regulations applicable to us such as the Foreign Corrupt Practices Act (the "FCPA") unfortunately are more commonplace. Although we have implemented policies and procedures with the intention of ensuring compliance with these laws and regulations, our employees, contractors and agents, as well as distributors and resellers involved in our international sales, may take actions in violation of our policies. Many of our vendors and strategic business allies also have international operations and are subject to the risks described above. Even if we are able to successfully manage the risks of international operations, our business may be adversely affected if one or more of our business partners are not able to successfully manage these risks. There can be no assurance that one or more of these factors will not have a material adverse effect on our business strategy and financial condition.

Foreign currency exchange rates may adversely affect our results.

We are exposed to market risk primarily related to foreign currencies and interest rates. In particular, we are exposed to changes in the value of the U.S. dollar versus the local currency in which our products are sold and our services are purchased, including devaluation and revaluation of local currencies. Accordingly, fluctuations in foreign currency rates could adversely affect our revenues.

In particular, the uncertainty with respect to the ability of certain European countries to continue to service their sovereign debt obligations and the related European financial restructuring efforts may cause the value of the Euro and other European currencies to fluctuate. If the value of European currencies, including the Euro, deteriorates, thus reducing the purchasing power of European customers, our sales could be adversely affected.

Risks Related to Regulatory Compliance and Legal Matters

Our inability to obtain appropriate industry certifications or approvals from governmental regulatory bodies could impede our ability to grow revenues in our wireless products.

The sale of our wireless products in some geographical markets is sometimes dependent on the ability to gain certifications and/or approvals by relevant governmental bodies. In addition, many of our products are certified as meeting various industry quality and/or compatibility standards. Failure to obtain these certifications or approvals, or delays in receiving any needed certifications or approvals, could impact our ability to compete effectively or at all in these markets and could have an adverse impact on our revenues.

Our failure to comply effectively with regulatory laws pertaining to our foreign operations could have a material adverse effect on our revenues and profitability.

We are required to comply with U.S. government export regulations in the sale of our products to foreign customers, including requirements to properly classify and screen our products against a denied parties list prior to shipment. We are also required to comply with the provisions of the FCPA and all other anti-corruption laws, such as the U.K. Anti-Bribery Act, of all other countries in which we do business, directly or indirectly, including compliance with the anti-bribery prohibitions and the accounting and recordkeeping requirements of these laws. Violations of the FCPA or other similar laws could trigger sanctions, including ineligibility for U.S. government insurance and financing, as well as large fines. Failure to comply with the aforementioned regulations could also affect our decision to sell our products in international jurisdictions, which could have a material adverse effect on our revenues and profitability.

Our failure to comply effectively with the requirements of applicable environmental legislation and regulation could have a material adverse effect on our revenues and profitability.

Certain states and countries have passed regulations relating to chemical substances in electronic products and requiring electronic products to use environmentally friendly components. For example, the European Union has the Waste Electrical and Electronic Equipment Directive, the Restrictions of Hazardous Substances Directive, and the Regulation on Registration, Evaluation, Authorization and Restriction of Chemicals. In the future, China and other countries including the U.S. are expected to adopt further environmental compliance programs. In order to comply with these regulations, we may need to redesign our products to use different components, which may be more expensive, if they are available at all. If we fail to comply with these regulations, we may not be able to sell our products in jurisdictions where these regulations apply, which could have a material adverse effect on our revenues and profitability.

Current or future litigation could adversely affect us.

We are subject to a wide range of claims and lawsuits in the course of our business. Any lawsuit may involve complex questions of fact and law and may require the expenditure of significant funds and the diversion of other resources. The results of litigation are inherently uncertain, and adverse outcomes are possible.

In particular, litigation regarding intellectual property rights occurs frequently in our industry. The results of litigation are inherently uncertain, and adverse outcomes are possible. Adverse outcomes may have a material adverse effect on our business, financial condition or results of operations.

There is a risk that other third parties could claim that our products, or our customers' products, infringe on their intellectual property rights or that we have misappropriated their intellectual property. In addition, software, business processes and other property rights in our industry might be increasingly subject to third-party infringement claims as the number of competitors grows and the functionality of products in different industry segments overlaps. Other parties might currently have, or might eventually be issued, patents that pertain to the proprietary rights we use. Any of these third parties might make a claim of infringement against us. The results of litigation are inherently uncertain, and adverse outcomes are possible.

Responding to any infringement claim, regardless of its validity, could:

- be time-consuming, costly and/or result in litigation;
- divert management's time and attention from developing our business;
- require us to pay monetary damages, including treble damages if we are held to have willfully infringed;
- require us to enter into royalty and licensing agreements that we would not normally find acceptable;
- require us to stop selling or to redesign certain of our products; or
- require us to satisfy indemnification obligations to our customers.

If any of these occur, our business, financial condition or results of operations could be adversely affected

General Risk Factors

If we are unable to attract, retain or motivate key senior management and technical personnel, it could seriously harm our business.

Our financial performance depends substantially on the performance of our executive officers and of key engineers, marketing and sales employees. We are particularly dependent upon our technical personnel, due to the specialized technical nature of our business. If we were to lose the services of our executive officers or any of our key personnel and were not able to find replacements in a timely manner, our business could be disrupted, other key personnel might decide to leave, and we might incur increased operating expenses associated with finding and compensating replacements.

Our quarterly operating results may fluctuate, which could cause the market price of our common stock to decline.

We have experienced, and expect to continue to experience, significant fluctuations in net revenue, expenses and operating results from quarter to quarter. We therefore believe that quarter to quarter comparisons of our operating results are not a good indication of our future performance, and you should not rely on them to predict our future operating or financial performance or the future performance of the market price of our common stock. A high percentage of our operating expenses are relatively fixed and are based on our forecast of future revenue. If we were to experience an unexpected reduction in net revenue in a quarter, we would likely be unable to adjust our short-term expenditures significantly. If this were to occur, our operating results for that fiscal quarter would be harmed. In addition, if our operating results in future fiscal quarters were to fall below the expectations of equity analysts and investors, the market price of our common stock would likely fall.

The market price of our common stock may be volatile based on a number of factors, many of which are not under our control.

The market price of our common stock has been highly volatile. The market price of our common stock could be subject to wide fluctuations in response to a variety of factors, many of which are out of our control, including:

- adverse changes in domestic or global economic, market and other conditions;
- new products or services offered by our competitors;
- our completion of or failure to complete significant one-time sales of our products;
- actual or anticipated variations in quarterly operating results;
- changes in financial estimates by securities analysts;
- announcements of technological innovations;
- our announcement of significant acquisitions, strategic partnerships, joint ventures or capital commitments;
- conditions or trends in the industry;
- additions or departures of key personnel;
- increased competition from industry consolidation;
- mergers and acquisitions; and
- sales of common stock by our stockholders or us or repurchases of common stock by us.

In addition, the Nasdaq Capital Market often experiences price and volume fluctuations. These fluctuations often have been unrelated or disproportionate to the operating performance of companies listed on the Nasdaq Capital Market.

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

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

Exhibit Number	Description	Provided Herewith	Incorporated by Reference		
			Form	Exhibit	Filing Date
3.1	Amended and Restated Certificate of Incorporation of Lantronix, Inc., as amended		10-K	3.1	08/29/2013
3.2	Amended and Restated Bylaws of Lantronix, Inc.		8-K	3.2	11/15/2012
10.1	Lease dated January 20, 2022 between Lantronix, Inc. and Jet 55 Property Owner LLC		8-K	10.1	1/26/2022
10.2	Second Amendment to Third and Restated Loan Security Agreement dated February 15, 2022, among Lantronix, Inc., Lantronix Holding Company, Lantronix Canada, ULC and Lantronix Technologies Canada (Taiwan) Ltd. and Transition Networks, Inc.		8-K	10.1	2/16/2022
31.1	Certification of Principal Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	X			
31.2	Certification of Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	X			
32.1*	Certification of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	X			
101.INS	Inline XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document	X			
101.SCH	Inline XBRL Taxonomy Extension Schema Document	X			
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document	X			
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document	X			
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase Document	X			
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document	X			
104	Cover Page Interactive Data File (formatted as inline XBRL and contained in Exhibit 101)				

* Furnished, not filed.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

LANTRONIX, INC.

Date: May 5, 2022

By: /s/ PAUL PICKLE
Paul Pickle
President and Chief Executive Officer
(Principal Executive Officer)

Date: May 5, 2022

By: /s/ JEREMY WHITAKER
Jeremy Whitaker
Chief Financial Officer
(Principal Financial and Accounting Officer)

**CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Paul Pickle, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Lantronix, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in the Securities Exchange Act of 1934, as amended, Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in the Securities Exchange Act of 1934, as amended, Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 5, 2022

/s/ Paul Pickle
Paul Pickle
President and Chief Executive Officer (Principal Executive Officer)

**CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

I, Jeremy Whitaker, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Lantronix, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in the Securities Exchange Act of 1934, as amended, Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in the Securities Exchange Act of 1934, as amended, Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 5, 2022

/s/ Jeremy Whitaker
Jeremy Whitaker
Chief Financial Officer
(Principal Financial and Accounting Officer)

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER
PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

The following certifications are being furnished solely to accompany the Quarterly Report on Form 10-Q for the quarterly period ended March 31, 2022 (the "Report") pursuant to U.S.C. Section 1350, and pursuant to SEC Release No. 33-8238 are being "furnished" to the Securities and Exchange Commission rather than "filed" either as part of the Report or as a separate disclosure statement, and are not to be incorporated by reference into the Report or any other filing of Lantronix, Inc. (the "Company"), whether made before or after the date hereof, regardless of any general incorporation language in such filing. The following certifications shall not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to liability under that section.

Certification of the Chief Executive Officer

Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned officer of the Company hereby certifies, to such officer's knowledge, that:

- (i) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results operations of the Company as of, and for, the periods presented in such Report.

Date: May 5, 2022

/s/ Paul Pickle
Paul Pickle
President and Chief Executive Officer
(Principal Executive Officer)

Certification of the Chief Financial Officer

Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned officer of the Company hereby certifies, to such officer's knowledge, that:

- (i) the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended; and
- (ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results operations of the Company as of, and for, the periods presented in such Report.

Date: May 5, 2022

/s/ Jeremy Whitaker
Jeremy Whitaker
Chief Financial Officer
(Principal Financial and Accounting Officer)