



Earnings Conference Call Presentation **Q2 2017**

August 8, 2017

Caution on Forward-Looking Statements

This presentation contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements can be identified by non-historical statements and often include words such as “outlook,” “potential,” “believes,” “expects,” “anticipates,” “estimates,” “intends,” “plans,” “seeks” or words of similar meaning, or future-looking or conditional verbs, such as “will,” “should,” “could,” “may,” “might,” “aims,” “intends,” or “projects.” These statements may include, but are not limited to, statements relating to: our business strategy; guidance or projections related to revenue, Adjusted EBITDA, bookings, and other measures of future economic performance; the contributions and performance of our businesses including acquired businesses and international operations; projections for future capital expenditures; and other guidance, projections, plans, objectives, and related estimates and assumptions. A forward-looking statement is neither a prediction nor a guarantee of future events or circumstances. In addition, forward-looking statements are based on the Company’s current assumptions, expectations and beliefs and are subject to certain risks and uncertainties that could cause actual results to differ materially from our present expectations or projections. Some important factors that could cause actual results, performance or achievement to differ materially from those expressed or implied by these forward-looking statements include, but are not limited to: the risk that we are unable to execute our business strategy; declining demand for our language learning solutions; the risk that we are not able to manage and grow our business; the impact of any revisions to our pricing strategy; the risk that we might not succeed in introducing and producing new products and services; the impact of foreign exchange fluctuations; the adequacy of internally generated funds and existing sources of liquidity, such as bank financing, as well as

our ability to raise additional funds; the risk that we cannot effectively adapt to and manage complex and numerous technologies; the risk that businesses acquired by us might not perform as expected; and the risk that we are not able to successfully expand internationally. We expressly disclaim any obligation to update or revise any forward-looking statements, whether as a result of new information, future developments or otherwise, except as required by law. These factors should not be construed as exhaustive and should be read in conjunction with the other cautionary statements, risks and uncertainties that are more fully described in the Company’s filings with the U.S. Securities and Exchange Commission (SEC), including those described under the section entitled “Risk Factors” in the Company’s most recent quarterly Form 10-Q filings and Annual Report on Form 10-K, as such factors may be updated from time to time.

Immaterial rounding differences may be present in this data in order to conform to reported totals.

Non-GAAP Financial Measures

Today’s presentation and discussion also contain references to non-GAAP financial measures. The full definition, GAAP comparisons, and reconciliation of those measures are available in this presentation or in our press release which is posted on our website at www.rosettastone.com. Our non-GAAP measures may not be comparable to those used by other companies, and we encourage you to review and understand all our financial reporting before making any investment decision.



Q2 2017 Highlights

10th consecutive quarter of Y/Y OPEX reductions

1 Revenue relatively flat Y/Y at \$45.9MM in 2Q17

2 OPEX decreased \$9.6MM or 20%Y/Y, representing the Company's 10th consecutive quarter of Y/Y expense reductions

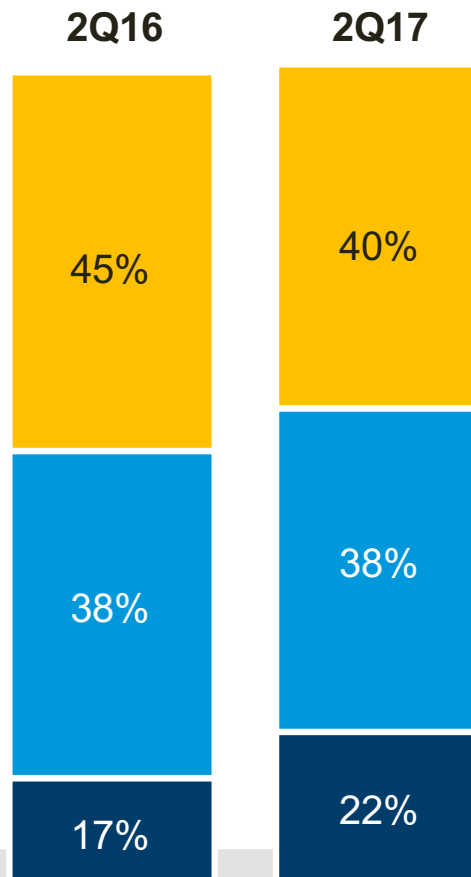
Total OPEX includes a \$2.9MM non-cash impairment charge in 2Q16 and restructuring costs of \$0.2MM and \$2.0MM of incurred in 2Q17 and 2Q16, respectively; net OPEX decreased \$4.8MM or 11% Y/Y

3 Net loss of \$1.1MM or \$(0.05) per diluted share, compared to net loss of \$9.0MM or \$(0.41) per diluted share in the year-ago period

4 Ended the quarter with zero debt and \$26.4MM in cash and cash equivalents at June 30, 2017

Continued Revenue Growth at Lexia

Percent of Revenue Mix



Consumer E&E Lexia

- Lexia revenue up 30% Y/Y to record high \$10.4MM; pro forma revenue of \$10.9MM, up \$1.7MM or 19% Y/Y
- E&E Language revenue of \$17.3MM, down \$0.2MM or 1% Y/Y
 - Markets retained increased \$0.6MM or 4% Y/Y
 - Markets exited declined \$0.8MM, or 35% Y/Y
- Consumer revenue of \$18.3MM, down \$2.0MM or 10% Y/Y
 - U.S. DTC SaaS unit mix of 66%, up from 26% in the year-ago period

Combined Lexia+E&E ARR Up 7% Y/Y

Consumer migration toward 100% SaaS yields record subscriber count

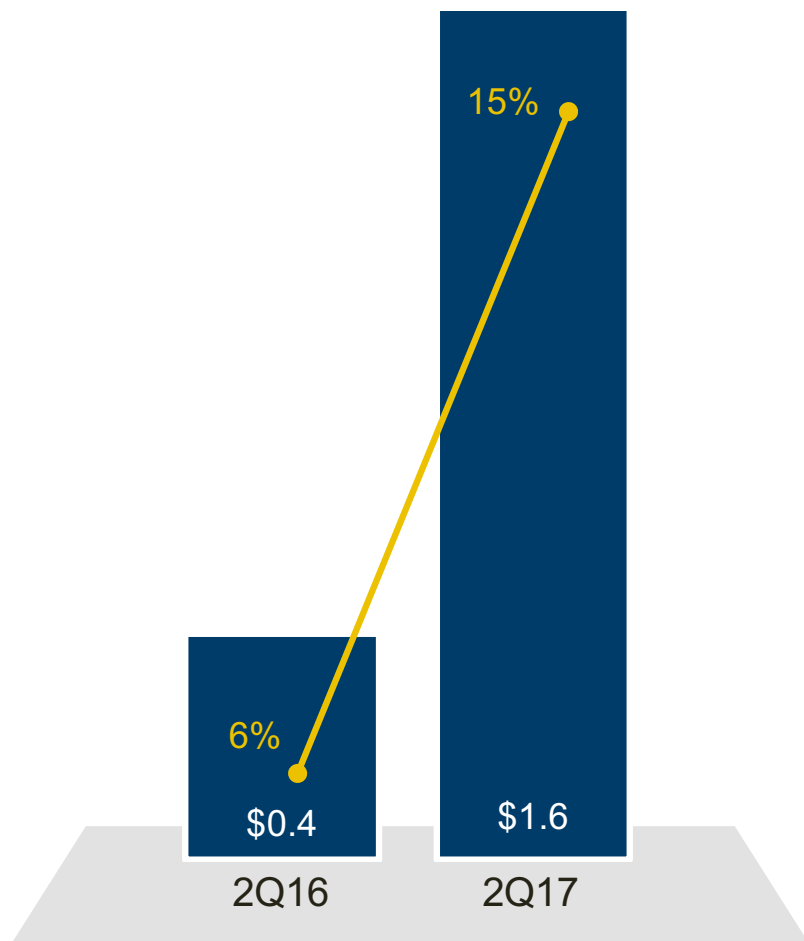
		2Q16A	2Q17A
Lexia	ARR (MM)	\$32.2	\$39.2
	Renewal Rate (TTM)	100%	85%
Enterprise and Education	ARR (MM)	\$58.7	\$58.4
	Renewal Rate (TTM)	75%	78%
Consumer	Paying Subscribers (000)	272	375

Lexia's renewal rate in 2Q17 was over 100%

Literacy Segment Contribution Margin¹ Up Y/Y

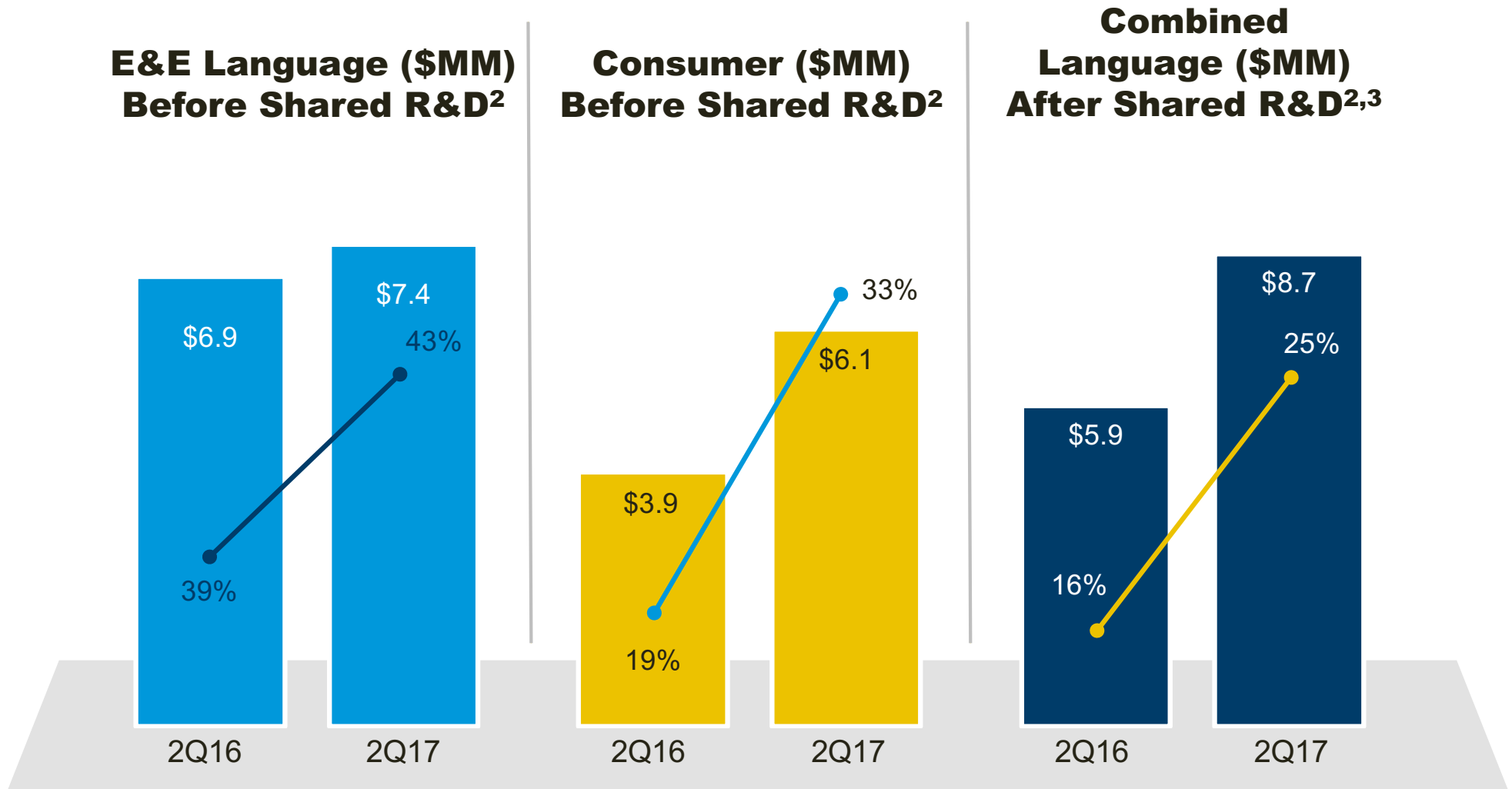
Results include increasing investments in infrastructure, product

Literacy (\$MM)²



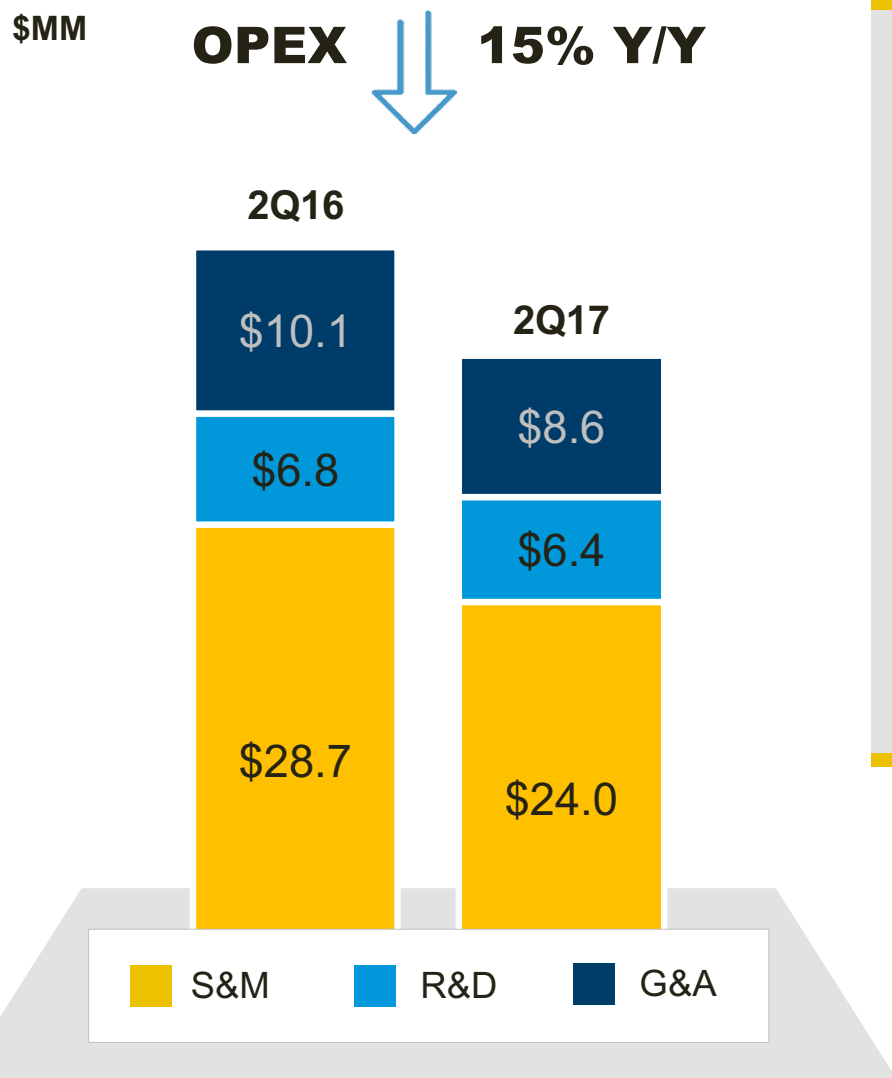
- Lexia segment contribution margin increased to \$1.6MM, up from \$0.4MM in the year-ago period
- Definition of segment contribution was revised in 1Q17; Literacy segment includes R&D expense²
- Margin percentage increased to 15% of revenue, up from 6% in the year-ago period
 - Pro forma segment contribution, which excludes the effects of purchase accounting, was \$2.1MM or 19% in 2Q17, compared to \$1.1MM or 12% in 2Q16

Language Segment Contribution Margin¹ Up Y/Y



¹ See appendix for revised definition of segment contribution margin; ² E&E Language and Consumer are shown before shared Language R&D expense; ³ Combined Language includes R&D expense of \$4.6MM in 2Q16 and \$4.3MM in 2Q17.

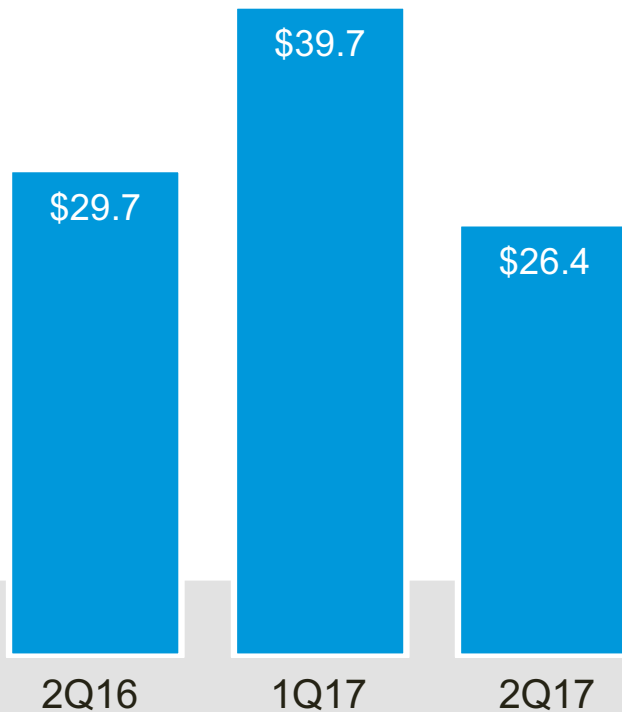
OPEX¹ Down Y/Y for 10th Consecutive Quarter



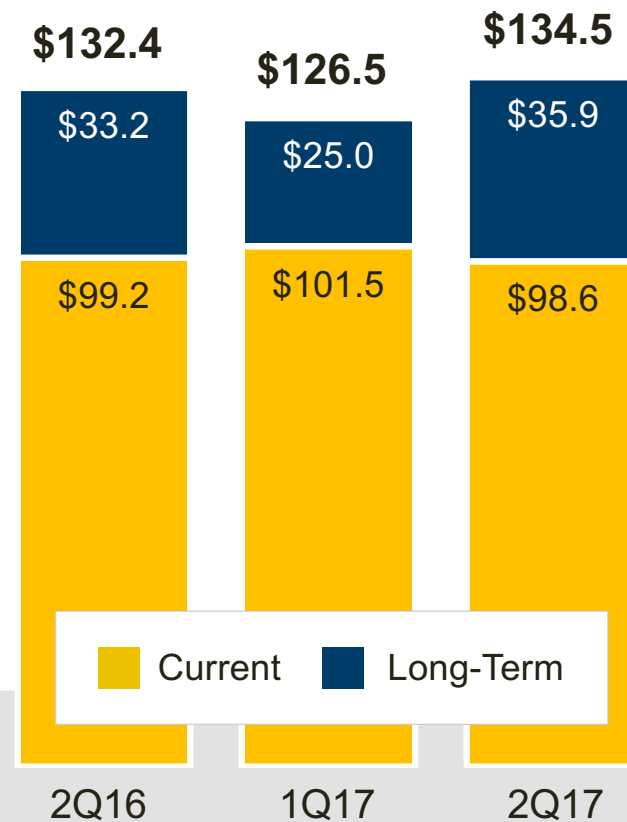
- The sum total of sales and marketing, research and development, and general and administrative expense was \$39.0MM in 2Q17 and \$45.6MM in 2Q16, a decline of \$6.6MM or 15% Y/Y
- S&M down \$4.7MM or 16% Y/Y
- R&D down \$0.4MM or 6% Y/Y
- G&A down \$1.5MM or 15% Y/Y

Seasonal Use of Cash in Q2, First Half

Cash and Cash Equivalents (\$MM)¹



Deferred Revenue (\$MM)²



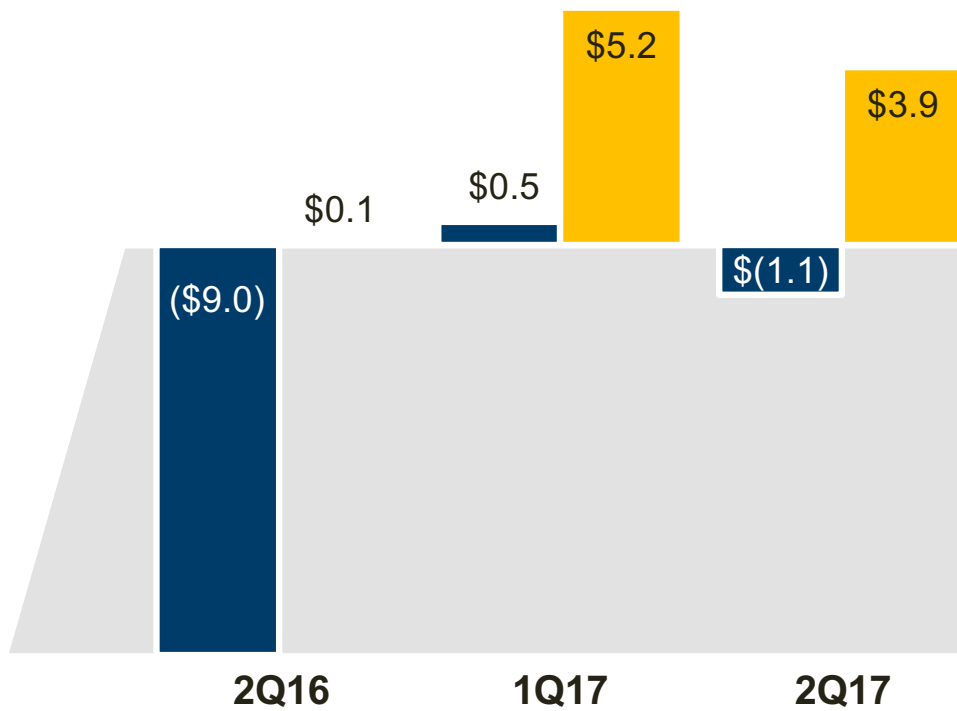
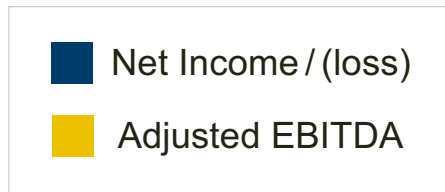
¹ Includes \$9.0MM in 1Q17 and \$2.5MM in 2Q17 received from SOURCENEXT.

² 2Q17 includes \$11.3MM from the SOURCENEXT transaction; \$10.7MM is L-T and \$0.6MM is S-T.

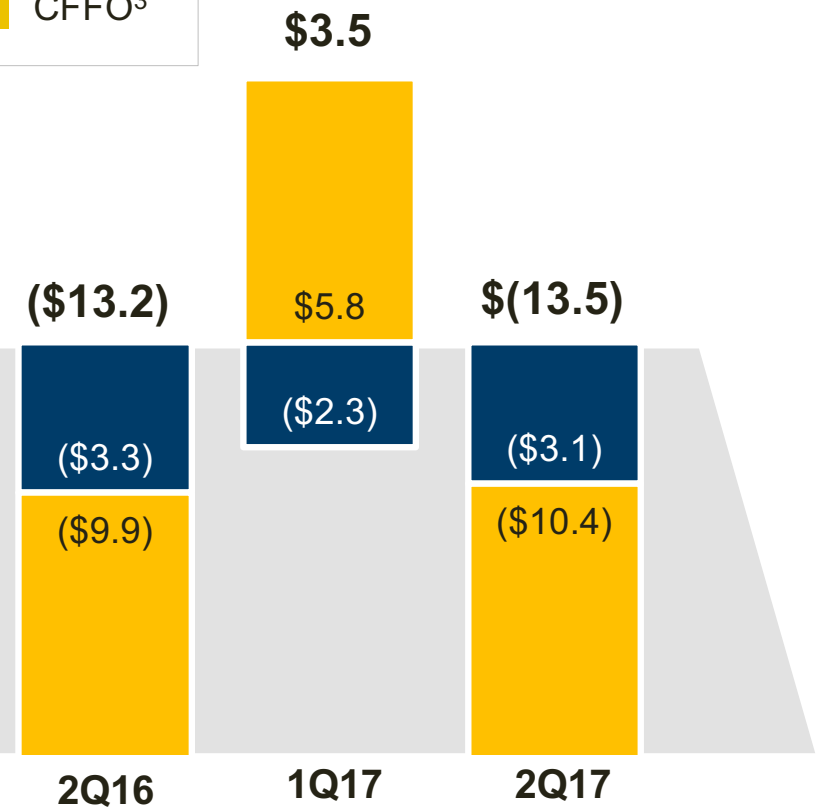


2Q17 Non-GAAP Financial Measures¹

Adjusted EBITDA (\$MM)¹



Free Cash Flow (\$MM)²



¹ See Appendix for definitions and reconciliation of GAAP to non-GAAP Financial Measures; ² CAPEX is 'Purchases of property and equipment'; ³ CFFO is 'Net cash provided by (used in) operating activities' from the Consolidated Statements of Cash Flows

Full Year 2017 Guidance

Revenue, GAAP net loss, Adj. EBITDA, year-end cash balance unchanged

Amounts in \$MM	FY16A	FY17E
GAAP Revenue	\$194.1	Approx. \$182 - \$185
GAAP Net Loss	\$(27.6)	Approx. \$(13 - 15)
Adjusted EBITDA ¹	\$4.4	Approx. \$8 - 10
Capital Expenditures	\$12.5	Approx. \$14
Year-End Cash Balance	\$36.2	Approx. \$44

¹ See Appendix for definitions and reconciliation of GAAP to non-GAAP Financial Measures.





Thank You.

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Appendix

Definitions of Statistical Measures

- Annualized recurring revenue (or “ARR”) is computed using the annualized value of active subscription arrangements at the end of the period. ARR is a performance metric used to assess the health and trajectory of our E&E Language and Literacy segments, which we believe aids investors in understanding our segment results. We present ARR as a statistical measure rather than a non-GAAP financial measure. ARR should be viewed independently of revenue and deferred revenue, as ARR is a performance metric and is not intended to be combined with either of these items.

Definitions of Non-GAAP Financial Measures

- **Bookings** represent executed sales contracts received by the Company that are either recorded immediately as revenue or as deferred revenue.
- **Adjusted EBITDA** is GAAP net income/loss plus interest income and expense, other income/expense, income tax benefit/expense, impairment, lease abandonment and termination, depreciation, amortization, stock-based compensation, restructuring, and strategy and cost-reduction related consulting expenses. In addition, Adjusted EBITDA excludes "Other" items related to non-restructuring wind down and severance costs, and transaction and other costs associated with mergers and acquisitions, as well as all adjustments related to recording the non-cash tax valuation allowance for deferred tax assets. Adjusted EBITDA for prior periods has been revised to conform to current definition.
- **Free cash flow** is cash flow from operating activities minus cash used in purchases of property and equipment.

Definitions of Non-GAAP Financial Measures

- **Segment contribution** is calculated as segment revenue less expenses directly incurred by or allocated to the segment. Direct segment expenses include costs and expenses that are directly incurred by or allocated to the segment and include materials costs, service costs, customer care and coaching costs, sales and marketing expenses, and bad debt expense. In addition to the previously referenced expenses, the Literacy segment includes direct research and development expenses and Combined Language includes shared research and development expenses, costs of revenue, sales and marketing, and general and administrative expenses applicable to the Consumer Language and Enterprise & Education Language segments.

Adjusted EBITDA and Free Cash Flow¹

	Amounts (\$000)						
	Quarterly				FY16	Quarterly	
	1Q16	2Q16	3Q16	4Q16		1Q17	2Q17
GAAP net income (loss)	\$ (7,507)	\$ (8,978)	\$ (5,452)	\$ (5,613)	\$ (27,550)	\$ 454	\$ (1,135)
Total non-operating (income) expense, net	(1,129)	(816)	(524)	596	(1,873)	(209)	(312)
Income tax (benefit) expense	449	(992)	1,793	1,253	2,503	700	782
Impairment	0	2,902	1,028	0	3,930	0	0
Depreciation and amortization	3,408	3,178	3,226	3,510	13,322	3,075	2,987
Stock-based compensation	421	1,397	1,639	1,449	4,906	147	1,359
Restructuring expenses	2,509	2,512	162	10	5,193	780	205
Lease abandonment and termination	0	30	0	1,614	1,644	0	0
Strategy consulting expense	402	519	458	577	1,956	169	0
Other EBITDA adjustments	(117)	304	85	56	328	39	16
Adjusted EBITDA	\$ (1,564)	\$ 56	\$ 2,415	\$ 3,452	\$ 4,359	\$ 5,155	\$ 3,902

	Amounts (\$000)						
	Quarterly				FY16	Quarterly	
	1Q16	2Q16	3Q16	4Q16		1Q17	2Q17
Net cash provided by/(used in) operating activities	\$ (2,546)	\$ (9,879)	\$ 6,479	\$ 7,186	\$ 1,240	\$ 5,769	\$ (10,397)
Purchases of property and equipment	(2,586)	(3,348)	(3,694)	(2,886)	(12,514)	(2,313)	(3,080)
Free Cash Flow	\$ (5,132)	\$ (13,227)	\$ 2,785	\$ 4,300	\$ (11,274)	\$ 3,456	\$ (13,477)



¹ See Appendix for definitions and reconciliation of GAAP to non-GAAP Financial Measures.

Revenue and Bookings¹

	Amounts (\$000)						
	Quarterly				FY16	Quarterly	
	1Q16	2Q16	3Q16	4Q16		1Q17	2Q17
Revenue							
Literacy	\$ 7,577	\$ 7,950	\$ 8,786	\$ 9,810	\$ 34,123	\$ 10,170	\$ 10,370
Enterprise & Education ("E&E") Language							
Enterprise	11,044	10,479	11,041	10,554	43,118	9,408	9,914
North America K-12	7,287	7,011	7,295	7,372	28,965	7,092	7,346
Total E&E Language	18,331	17,490	18,336	17,926	72,083	16,500	17,260
Consumer	22,094	20,276	21,571	23,942	87,883	21,023	18,275
Total Revenue	\$ 48,002	\$ 45,716	\$ 48,693	\$ 51,678	\$ 194,089	\$ 47,693	\$ 45,905
Bookings							
Literacy	\$ 3,817	\$ 9,433	\$ 17,923	\$ 7,221	\$ 38,394	\$ 5,300	\$ 8,628
Enterprise & Education ("E&E") Language							
Enterprise	7,906	8,972	12,553	11,071	40,502	6,034	10,203
North America K-12	2,877	9,184	11,643	5,438	29,142	2,890	8,354
Total E&E Language	10,783	18,156	24,196	16,509	69,644	8,924	18,557
Consumer	22,911	18,234	19,203	24,413	84,761	18,495	27,299
Total Bookings	\$ 37,511	\$ 45,823	\$ 61,322	\$ 48,143	\$ 192,799	\$ 32,719	\$ 54,484



¹ See Appendix for definitions and reconciliation of GAAP to non-GAAP Financial Measures.

Reconciliation of Revenue and Bookings¹

	Amounts (\$000)						
	Quarterly				FY16	Quarterly	
	1Q16	2Q16	3Q16	4Q16		1Q17	2Q17
Reconciliation of Revenue to Bookings							
Literacy							
Segment revenue	\$ 7,577	\$ 7,950	\$ 8,786	\$ 9,810	\$ 34,123	\$ 10,170	\$ 10,370
Segment change in deferred revenue	(3,760)	1,483	9,137	(2,589)	4,271	(4,870)	(1,742)
Bookings	\$ 3,817	\$ 9,433	\$ 17,923	\$ 7,221	\$ 38,394	\$ 5,300	\$ 8,628
Enterprise & Education ("E&E") Language							
Segment revenue	\$ 18,331	\$ 17,490	\$ 18,336	\$ 17,926	\$ 72,083	\$ 16,500	\$ 17,260
Segment change in deferred revenue	(7,548)	666	5,860	(1,417)	(2,439)	(7,576)	1,297
Bookings	\$ 10,783	\$ 18,156	\$ 24,196	\$ 16,509	\$ 69,644	\$ 8,924	\$ 18,557
Consumer							
Segment revenue	\$ 22,094	\$ 20,276	\$ 21,571	\$ 23,942	\$ 87,883	\$ 21,023	\$ 18,275
Segment change in deferred revenue	817	(2,042)	(2,368)	471	(3,122)	(2,528)	9,024
Bookings	\$ 22,911	\$ 18,234	\$ 19,203	\$ 24,413	\$ 84,761	\$ 18,495	\$ 27,299
Total revenue	\$ 48,002	\$ 45,716	\$ 48,693	\$ 51,678	\$ 194,089	\$ 47,693	\$ 45,905
Change in deferred revenue	(10,491)	107	12,629	(3,535)	(1,290)	(14,974)	8,579
Total bookings	\$ 37,511	\$ 45,823	\$ 61,322	\$ 48,143	\$ 192,799	\$ 32,719	\$ 54,484



¹ See Appendix for definitions and reconciliation of GAAP to non-GAAP Financial Measures.

Segment Contribution¹

	Amounts (\$000)						
	Quarterly				FY16	Quarterly	
	1Q16	2Q16	3Q16	4Q16		1Q17	2Q17
Revenue:							
Literacy segment	\$ 7,577	\$ 7,950	\$ 8,786	\$ 9,810	\$ 34,123	\$ 10,170	\$ 10,370
Enterprise & Education ("E&E") Language segment	18,331	17,490	18,336	17,926	72,083	16,500	17,260
Consumer segment	22,094	20,276	21,571	23,942	87,883	21,023	18,275
Shared services	0	0	0	0	0	0	0
Combined Language	40,425	37,766	39,907	41,868	159,966	37,523	35,535
Total revenue	\$ 48,002	\$ 45,716	\$ 48,693	\$ 51,678	\$ 194,089	\$ 47,693	\$ 45,905
Segment contribution:							
Literacy segment	\$ 57	\$ 439	\$ (364)	\$ 1,400	\$ 1,532	\$ 961	\$ 1,591
E&E Language segment	6,297	6,903	8,064	7,818	29,082	7,119	7,357
Consumer segment	5,040	3,934	6,233	6,295	21,502	8,357	6,060
Shared services	(5,457)	(4,982)	(4,758)	(5,562)	(20,759)	(4,990)	(4,672)
Combined Language	5,880	5,855	9,539	8,551	29,825	10,486	8,745
Total segment contribution	\$ 5,937	\$ 6,294	\$ 9,175	\$ 9,951	\$ 31,357	\$ 11,447	\$ 10,336
Segment contribution margin percentage:							
Literacy segment	1%	6%	-4%	14%	4%	9%	15%
E&E Language segment	34%	39%	44%	44%	40%	43%	43%
Consumer segment	23%	19%	29%	26%	24%	40%	33%

¹ Please see the Appendix for definitions of non-GAAP financial measures. The Literacy segment was previously a component of the "Enterprise & Education" segment and is comprised solely of the Lexia business. Prior periods have been reclassified to reflect our current segment presentation and definition of segment contribution.





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