Rosetta Stone Inc. – Prepared Remarks
Third Quarter 2017

Rosetta Stone has prepared the following remarks regarding the results for the third quarter ended September 30, 2017, to provide shareholders and analysts more detail to help understand and analyze our results in conjunction with our earnings release, conference call and supplemental earnings slides. **These prepared remarks will not be read on the conference call.**

The conference call will begin at 5:00 p.m. ET on Thursday, November 2, 2017, and will include brief opening comments followed by questions and answers. Investors may dial into the live conference call using 1-778-331-2160 (toll/international) or 1-855-327-6837 (toll-free). A live webcast will also be available in the investor relations section of the Company's website at http://investors.rosettastone.com. A replay will be made available soon after the live conference call is completed and will remain available until midnight on November 9. Investors may dial into the replay using 1-412-317-6671 and passcode 10003711.

Please see the section "Definition of Non-GAAP Financial Measures" at the end of this document for an explanation of what our non-GAAP financial measures are and how they are computed.

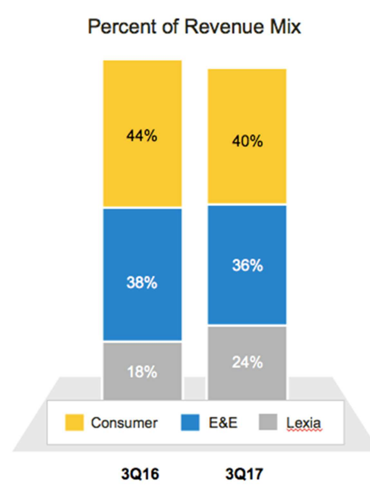
Q3 2017 Highlights

1. **Revenue at Lexia up 26% Y/Y to a record high $11.0MM in 3Q17**
2. **OPEX decreased $5.4MM or 12%Y/Y, reflecting 13% lower sales & marketing expense and 9% lower general & administrative expense**

   Total OPEX includes a $1.0MM non-cash impairment charge in 3Q16 and restructuring costs of $0.2MM and $0.2MM incurred in 3Q17 and 3Q16, respectively; net OPEX decreased $4.3MM or 10% Y/Y
3. **Net loss of $3.2MM or $(0.14) per diluted share, compared to net loss of $5.5MM or $(0.25) per diluted share in the year-ago period**
4. **Ended the quarter with zero debt and $40.1MM in cash and cash equivalents at September 30, 2017**

Q3 2017 Revenue

Total revenue declined $2.5 million (or 5%) year-over-year, to $46.2 million.



- Consumer segment revenue declined 14% year-over-year to $18.6 million, in part due to the continued transition of the segment to subscription-based sales from the sale of perpetual products and in part due to a decline in marketing spend. In addition, revenues in our retail channel declined as our terms retailers managed inventories down in advance of moving to consignment in Q4.
- E&E Language revenue declined 10% year-over-year to $16.5 million, driven by a 13% decline in the Enterprise category – both in the U.S. and in Europe – partially due to geographies and customer lines exited in 2016 as part of our refocusing of

the E&E business, which contributed to the $4.4 million or 18% decline in sales year-over-year. The decline in sales was also impacted by the sale in the third quarter of 2016 of two large multi-year deals totaling almost $2 million that were not available for renewal this year and by the deferral of certain expected new and renewal opportunities from the third quarter to the fourth quarter this year.

- Lexia revenue was a record high $11.0 million, up 26% year-over-year, as bookings grew 39% to $24.9 million, which was also a new high in quarterly bookings, as the carryover of pending deals at the end of June – along with the transition to more direct sales – produced great results in their seasonally strong third quarter. A new large 'win' for Lexia during the third quarter represented approximately $2.3 million and encompassed approximately 190 schools. As a reminder, Lexia's results include the impact of purchase accounting on acquired deferred revenue. Adjusting for this impact, Lexia's pro forma revenue was $11.4 million in Q3 2017 compared to $9.7 million in the same year-ago quarter, and Lexia's pro forma revenue growth was 17% year-over-year. The effect of purchase accounting has diminished over time and is not expected to be significant beyond 2017, therefore the Company intends to discontinue reporting this information after Q4 2017.

Q3 2017 Net Loss

The net loss improved 41% year-over-year to $3.2 million or 14-cents per diluted share. In the year-ago period, the net loss totaled $5.5 million, or 25-cents per diluted share. The net loss this quarter included a non-cash, pre-tax charge of $1.9 million for the write-off of CD box inventory at certain of our Retail partners as they transition to the new SaaS box product we discussed last quarter, and pre-tax charges of $0.2 million for restructuring; the net loss in the year-ago period included pre-tax charges of $0.2 million for restructuring and a non-cash $1.0 million charge for impairment.

Annualized Recurring Revenue

Q3 2017 ARR Performance Metrics

	Q3 2017	**Q3 2016**
Literacy	$42.2MM	$34.9MM
E&E Language	$56.9MM	$60.0MM

Annualized Recurring Revenue – or "ARR" – which is computed using the annualized value of subscriptions at the end of the period, separate from services like training and implementation. ARR is a performance metric used to assess the health and trajectory of our E&E Language and Literacy segments, which we believe cuts through the differences in the types of licenses and deal sizes in our businesses and aids 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.

ARR for the Literacy segment at September 30th was $42.2 million, which was up 21% year-over-year, reflecting the continuing growth in this business driven by high retention and renewal rates and new sales from its direct salesforce. ARR in the E&E Language segment at September 30th was approximately $56.9 million, which was down 5% year-over-year. The E&E Language ARR reflects, in part, our decision to exit direct sales in certain customer lines and geographies in 2016.

Segment Contribution

The Literacy segment contribution was $0.6 million (or 5% of segment revenue) in the third quarter 2017, compared to negative $0.4 million in the year-ago period. This improvement was due to higher revenue driven by an increase in sales, partially offset by higher expenses due to investments in Lexia's direct sales and marketing and R&D.

One note of clarification about the segment contribution data for the E&E Language segment, the Consumer segment and these two Language segments combined. Language Research & Development (R&D) expense is a shared service cost that is not allocated to either segment, but *is* included in combined Language – therefore, it is the combined Language view that is comparable to the Lexia segment contribution.

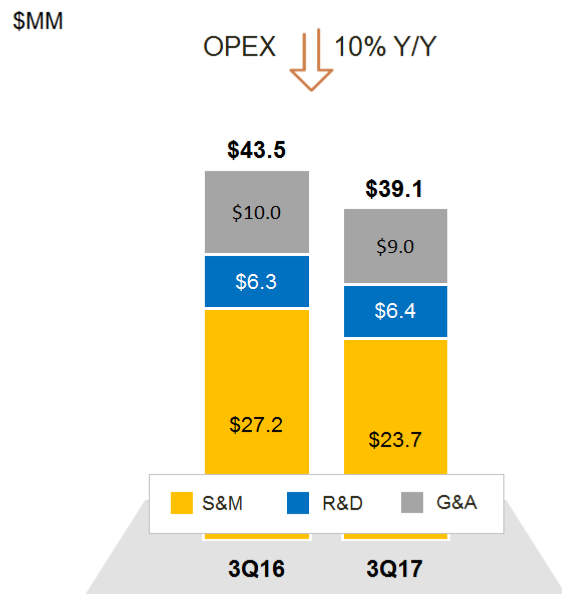
The combined Language segments contribution was $8.7 million (25% of total combined Language segments revenue) in Q3 2017, which was down from $9.5 million (24% of combined Language segments revenue) in Q3 2016. The decrease of $0.8 million was driven by higher Consumer Cost of Goods Sold (COGS) due to the $1.9 million non-cash charge for the write-off of the Retail CD box inventory discussed previously. Lower revenue in the combined Language segments reflects the shift of Consumer to subscription-based sales from perpetual sales and the strategic decision to exit certain customer lines and geographies (which was partially offset by lower sales and marketing expenses in both segments).

The E&E Language segment contribution margin before shared Language R&D expense decreased by $0.9 million to $7.2 million (or 43% of segment revenue), from $8.1 million (or 44% of segment revenue) in the year-ago period. This performance was driven by lower revenue partially due to geographies exited on a direct basis in 2016, partially offset by a 9% reduction in direct operating expenses.

Consumer Language segment contribution margin before shared Language R&D expense was $5.7 million (or 30% of segment revenue), which was down $0.5 million year-over-year compared to $6.2 million (or 29% of segment revenue) in the year-ago period. The performance reflected lower revenue as the result of the shift to subscription-based sales from perpetual product sales and higher cost of product revenue due to the $1.9 million non-cash charge for the write-off of the Retail CD box inventory discussed – both of which were nearly offset by a $3.6 million (or 30%) reduction in Consumer segment sales and marketing expenses as our marketing efficiency improved. Before the $1.9 million non-cash write-off for Retail CD inventory, the Consumer Q3 2017 segment margin was 41%.

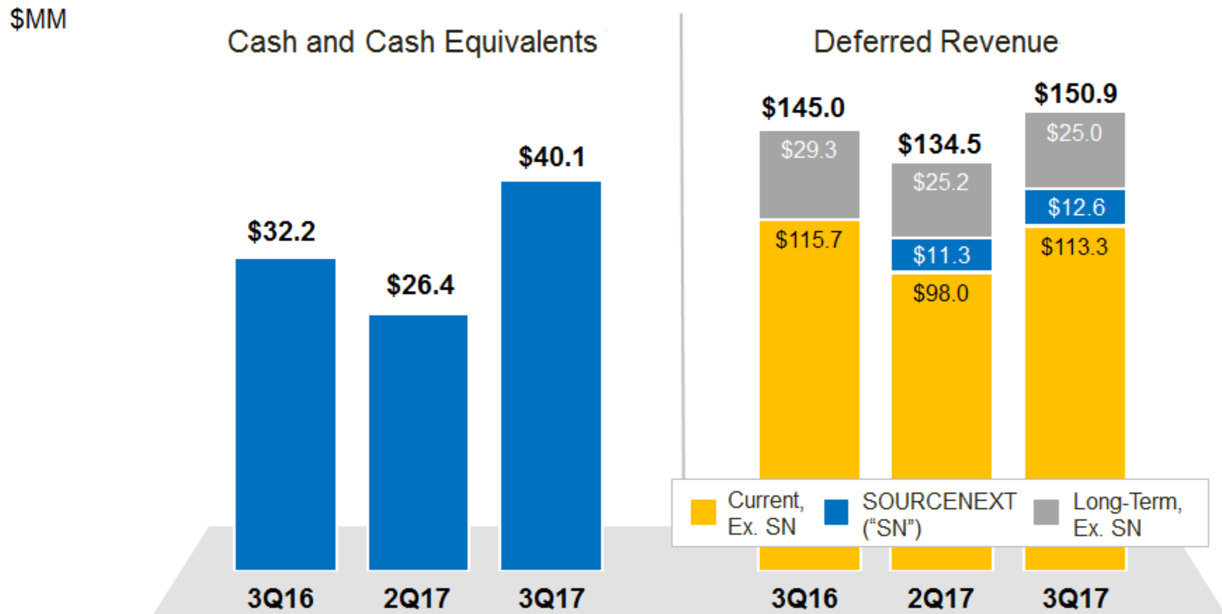
Q3 2017 Operating Expenses

Combined sales and marketing, research and development, and general and administrative expenses declined $4.4 million or 10% year-over-year in the third quarter – extending the trend to eleven consecutive quarters of year-over-year improvement, even as we continue to increase our investments in Lexia. G&A expense was down 9% year-over-year, while sales and marketing expense was down $3.5 million (or 13%) year-over-year; research and



development expense totaled $6.4 million, which was flat year-over-year.

Q3 2017 Selected Balance Sheet Data



Deferred revenue totaled $150.9 million at September 30, 2017, an increase of $9.4 million since December 31, 2016, and an increase of $5.9 million year-over-year. The balance included $1.5 million received this quarter reflecting the final significant up-front payment from our long-term licensing agreement with SOURCENEXT in Japan. Of the September 2017 total deferred revenue balance, $113.9 million (or approximately 76%), was short-term and will be recognized as revenue over the next 12 months.

We ended the third quarter with zero debt and $40.1 million of cash and cash equivalents. The ending cash balance was up $7.9 million compared to the third quarter last year, and up $13.8 million sequentially from June 30, 2017. The $1.5 million received from SOURCENEXT this quarter ($13.0 million year-to-date) also contributed to our Q3 ending cash balance.

Q3 2017 Non-GAAP Financial Measures

The reconciliation of the GAAP metrics to the non-GAAP financial measures can be found at the end of this document. Starting with Adjusted EBITDA, Q3 2017 net loss totaled $3.2 million, compared to the net loss of $5.5 million in the year-ago period. As a reminder, the net loss in Q3 2016 included pre-tax restructuring and impairment charges totaling $1.2 million. Adjusted EBITDA was positive $2.7 million, a $0.3 million improvement compared to $2.4 million in the year-ago period. Note that the $1.9 million inventory obsolescence charge incurred in Q3 2017 is not added back to this Adjusted EBITDA amount.

Net cash provided by operating activities totaled $17.3 million in the third quarter 2017, compared to $6.5 million in the same quarter last year. Capital expenditures, which primarily relate to capitalized labor on product and IT projects, totaled $3.5 million, compared to $3.7 million in the third quarter last year. Lexia drove the increase year-over-year, reflecting the heightened level of investment we are making to support their growth over the long-term. Free cash flow was positive $13.8 million in the third quarter, up from positive $2.8 million in the year-ago period, reflecting the lower net loss, working capital changes, the $1.5 million received from SOURCENEXT, and a reduction in capital expenditures. As a reminder, Q3 2016 included $3.9 million of cash payments related to the restructuring and the adjustment to the suggested retail value of our Consumer products (the adjustment to the suggested retail value of our Consumer products was expensed in Q2 2016).

2017 Financial Outlook

With respect to full year 2017 guidance, we are raising our guidance for total revenue, GAAP net loss and Adjusted EBITDA. We are maintaining our guidance for capital expenditures and the year-end cash balance. We now expect total consolidated revenue will be approximately $184 to $187 million, up from our previously stated range of approximately $182 to $185 million; our outlook for the mix among the three segments has changed slightly:

- Lexia revenue is now expected to be slightly above the $43 million previously guided, while Lexia bookings growth is projected to be 23% to 25%, which is toward the higher end of the 20% to 25% we guided to previously.
- We now expect E&E Language revenue to be approximately $68 million, as compared to our prior view of approaching $70 million.
- Consumer revenue is now expected to be approximately $75 million, up from our previously stated range of approximately $70 to $72 million.

The Consumer revenue outlook now includes the impact of approximately $2.0 million for returns as we move our terms Retail channel partners from terms to consignment (note that this is in addition to the $1.9 million charge to COGS for consignment partner returns taken in Q3 2017, as described above); we also currently anticipate approximately $2.0 million in lower revenues year-over-year due to an increase in the unit mix of SaaS-based subscriptions in our Retail channels, which is anticipated in Q4. We now expect the cash impact of the retail SaaS transition items in Consumer will be approximately $4.0 million, with approximately $2.0 million expected to be incurred in Q4 and another $2.0 million early in FY 2018. Our outlook for these impacts has changed due to reductions in Retail channel inventories that have already been realized, which is reflected in the lower revenues during the year as our Retail channel partners ordered less inventory in preparation for the change, offsetting the now lower than previously expected impacts. Finally, we now expect Consumer subscriptions will increase to approximately 55% of the new units sold this year, compared to 26% in 2016.

For the full year 2017, our outlook for the GAAP net loss has improved and we now expect it will be a loss of approximately $10 to $12 million, as compared to our previously stated range of approximately $13 to $15 million. Similarly, our outlook for positive Adjusted EBITDA has improved to approximately $10 to $12 million, which is up from our prior guidance of approximately $8 to $10 million. As a reminder, our full year 2017 outlook represents a significant increase over the $4.4 million Adjusted EBITDA achieved in 2016.

Our full-year outlook for cash has not changed and we continue to expect to end the year with approximately $44 million in cash and no debt. Note that we have received all of the $13 million in up-front payments from our long-term licensing agreement with SOURCENEXT, which we had anticipated in our prior cash estimates. Finally, we continue to expect capital expenditures to approach $14 million for the full year ended 2017.

Definitions

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.

Non-GAAP Financial Measures

- **Bookings** (or "Sales") 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.
- **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.
- **Segment free cash flow** is Adjusted EBITDA plus the change in deferred revenue, less the change in deferred commissions, less capital expenditures.

Adjusted EBITDA and Free Cash Flow[1]

	Amounts ($000)							
	Quarterly					Quarterly		
	1Q16	2Q16	3Q16	4Q16	FY16	1Q17	2Q17	3Q17
GAAP net income (loss)	$ (7,507)	$ (8,978)	$ (5,452)	$ (5,613)	$ (27,550)	$ 454	$ (1,135)	$ (3,231)
Total non-operating (income) expense, net	(1,129)	(816)	(524)	596	(1,873)	(209)	(312)	40
Income tax (benefit) expense	449	(992)	1,793	1,253	2,503	700	782	879
Impairment	0	2,902	1,028	0	3,930	0	0	0
Depreciation and amortization	3,408	3,178	3,226	3,510	13,322	3,075	2,987	3,015
Stock-based compensation	421	1,397	1,639	1,449	4,906	147	1,359	1,552
Restructuring expenses	2,509	2,512	162	10	5,193	780	205	196
Lease abandonment and termination	0	30	0	1,614	1,644	0	0	0
Strategy consulting expense	402	519	458	577	1,956	169	0	0
Other EBITDA adjustments	(117)	304	85	56	328	39	16	248
Adjusted EBITDA	$ (1,564)	$ 56	$ 2,415	$ 3,452	$ 4,359	$ 5,155	$ 3,902	$ 2,699

	Amounts ($000)							
	Quarterly					Quarterly		
	1Q16	2Q16	3Q16	4Q16	FY16	1Q17	2Q17	3Q17
Net cash provided by/(used in) operating activities	$ (2,546)	$ (9,879)	$ 6,479	$ 7,186	$ 1,240	$ 5,769	$ (10,397)	$ 17,305
Purchases of property and equipment	(2,586)	(3,348)	(3,694)	(2,886)	(12,514)	(2,313)	(3,080)	(3,510)
Free Cash Flow	$ (5,132)	$ (13,227)	$ 2,785	$ 4,300	$ (11,274)	$ 3,456	$ (13,477)	$ 13,795

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

Revenue and Bookings[1]

	Amounts ($000)							
	Quarterly					Quarterly		
	1Q16	2Q16	3Q16	4Q16	FY16	1Q17	2Q17	3Q17
Revenue								
Literacy	$ 7,577	$ 7,950	$ 8,786	$ 9,810	$ 34,123	$ 10,170	$ 10,370	$ 11,028
Enterprise & Education ("E&E") Language								
Enterprise	11,044	10,479	11,041	10,554	43,118	9,408	9,914	9,602
North America K-12	7,287	7,011	7,295	7,372	28,965	7,092	7,346	6,927
Total E&E Language	18,331	17,490	18,336	17,926	72,083	16,500	17,260	16,529
Consumer Language	22,094	20,276	21,571	23,942	87,883	21,023	18,275	18,649
Total Revenue	**$ 48,002**	**$ 45,716**	**$ 48,693**	**$ 51,678**	**$ 194,089**	**$ 47,693**	**$ 45,905**	**$ 46,206**
Bookings								
Literacy	$ 3,817	$ 9,433	$ 17,923	$ 7,221	$ 38,394	$ 5,300	$ 8,628	$ 24,878
Enterprise & Education ("E&E") Language								
Enterprise	7,906	8,972	12,553	11,071	40,502	6,034	10,203	9,610
North America K-12	2,877	9,184	11,643	5,438	29,142	2,890	8,354	10,224
Total E&E Language	10,783	18,156	24,196	16,509	69,644	8,924	18,557	19,834
Consumer Language	22,911	18,234	19,203	24,413	84,761	18,495	27,299	17,840
Total Bookings	**$ 37,511**	**$ 45,823**	**$ 61,322**	**$ 48,143**	**$ 192,799**	**$ 32,719**	**$ 54,484**	**$ 62,552**

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

Reconciliation of Revenue and Bookings[1]

Amounts ($000)	1Q16	2Q16	3Q16	4Q16	FY16	1Q17	2Q17	3Q17
	Quarterly					Quarterly		
Reconciliation of Revenue to Bookings								
Literacy								
Segment revenue	$ 7,577	$ 7,950	$ 8,786	$ 9,810	$ 34,123	$ 10,170	$ 10,370	$ 11,028
Segment change in deferred revenue	(3,760)	1,483	9,137	(2,589)	4,271	(4,870)	(1,742)	13,850
Bookings	$ 3,817	$ 9,433	$ 17,923	$ 7,221	$ 38,394	$ 5,300	$ 8,628	$ 24,878
Enterprise & Education ("E&E") Language								
Segment revenue	$ 18,331	$ 17,490	$ 18,336	$ 17,926	$ 72,083	$ 16,500	$ 17,260	$ 16,529
Segment change in deferred revenue	(7,548)	666	5,860	(1,417)	(2,439)	(7,576)	1,297	3,305
Bookings	$ 10,783	$ 18,156	$ 24,196	$ 16,509	$ 69,644	$ 8,924	$ 18,557	$ 19,834
Consumer Language								
Segment revenue	$ 22,094	$ 20,276	$ 21,571	$ 23,942	$ 87,883	$ 21,023	$ 18,275	$ 18,649
Segment change in deferred revenue	817	(2,042)	(2,368)	471	(3,122)	(2,528)	9,024	(809)
Bookings	$ 22,911	$ 18,234	$ 19,203	$ 24,413	$ 84,761	$ 18,495	$ 27,299	$ 17,840
Total revenue	**$ 48,002**	**$ 45,716**	**$ 48,693**	**$ 51,678**	**$ 194,089**	**$ 47,693**	**$ 45,905**	**$ 46,206**
Change in deferred revenue	(10,491)	107	12,629	(3,535)	(1,290)	(14,974)	8,579	16,346
Total bookings	**$ 37,511**	**$ 45,823**	**$ 61,322**	**$ 48,143**	**$ 192,799**	**$ 32,719**	**$ 54,484**	**$ 62,552**

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

Segment Contribution[1]

	Amounts ($000)							
	Quarterly					Quarterly		
	1Q16	2Q16	3Q16	4Q16	FY16	1Q17	2Q17	3Q17
Revenue:								
Literacy segment	$ 7,577	$ 7,950	$ 8,786	$ 9,810	$ 34,123	$ 10,170	$ 10,370	$ 11,028
Enterprise & Education ("E&E") Language segment	18,331	17,490	18,336	17,926	72,083	16,500	17,260	16,529
Consumer Language segment	22,094	20,276	21,571	23,942	87,883	21,023	18,275	18,649
Shared services	0	0	0	0	0	0	0	0
Combined Language	40,425	37,766	39,907	41,868	159,966	37,523	35,535	35,178
Total revenue	$ 48,002	$ 45,716	$ 48,693	$ 51,678	$ 194,089	$ 47,693	$ 45,905	$ 46,206
Segment contribution:								
Literacy segment	$ 57	$ 439	$ (364)	$ 1,400	$ 1,532	$ 961	$ 1,591	$ 582
E&E Language segment	6,297	6,903	8,064	7,818	29,082	7,119	7,357	7,176
Consumer Language segment	5,040	3,934	6,233	6,295	21,502	8,357	6,060	5,683
Shared services	(5,457)	(4,982)	(4,758)	(5,562)	(20,759)	(4,990)	(4,672)	(4,148)
Combined Language	5,880	5,855	9,539	8,551	29,825	10,486	8,745	8,711
Total segment contribution	$ 5,937	$ 6,294	$ 9,175	$ 9,951	$ 31,357	$ 11,447	$ 10,336	$ 9,293
Segment contribution margin percentage:								
Literacy segment	1%	6%	-4%	14%	4%	9%	15%	5%
E&E Language segment	34%	39%	44%	44%	40%	43%	43%	43%
Consumer Language segment	23%	19%	29%	26%	24%	40%	33%	30%

[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.