QUICKLOGIC CORPORATION
Form 10-Q
August 10, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

(Mark One)

[x] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934
For the Quarterly Period Ended July 1, 2018

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: 000-22671

QUICKLOGIC CORPORATION

(Exact name of registrant as specified in its charter)

DELAWARE	77-0188504
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1277 ORLEANS DRIVE, SUNNYVALE, CA 94089

(Address of principal executive offices, including Zip Code)

(408) 990-4000

(Registrant's telephone number, including area code)

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 [x]   No [ ]

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted 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 and post such files).   Yes [x]   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 definition of “large accelerated filer,” “accelerated filer”, “smaller reporting company” and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	[ ]		Accelerated Filer	[x]
Non-accelerated filer	[ ]	(Do not check if a smaller reporting company)	Smaller Reporting Company	[ ]
Emerging growth 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 in Rule 12b-2 of the Securities Exchange Act).   Yes [ ]   No [x]

As of August 3, 2018, the registrant had outstanding 94,581,143 shares of common stock, par value $0.001.

QUICKLOGIC CORPORATION

FORM 10-Q

July 1, 2018

PART I. Financial Information

Item 1. Financial Statements

QUICKLOGIC CORPORATION

UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands, except par value amount)

	July 1, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$22,815	$16,527
Accounts receivable, net of allowances for doubtful accounts of $0 and $0	2,191	925
Inventories	4,290	3,559
Other current assets	1,099	997
Total current assets	30,395	22,008
Property and equipment, net	1,790	2,375
Other assets	246	253
TOTAL ASSETS	$32,431	$24,636
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Revolving line of credit	$6,000	$6,000
Trade payables	1,700	1,437
Accrued liabilities	1,828	1,653
Current portion of capital lease obligations	303	299
Total current liabilities	9,831	9,389
Long-term liabilities:		
Capital lease obligations, less current portion	115	355
Other long-term liabilities	61	14
Total liabilities	10,007	9,758
Commitments and contingencies (see Note 12)		
Stockholders' equity:		
Preferred stock, $0.001 par value; 10,000 shares authorized; no shares issued and outstanding	—	—
Common stock, $0.001 par value; 200,000 authorized; 94,575 and 80,536 shares issued and outstanding as of July 1, 2018 and December 31, 2017, respectively	95	80
Additional paid-in capital	283,819	268,833
Accumulated deficit	(261,490)	(254,035)
Total stockholders' equity	22,424	14,878
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$32,431	$24,636

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

QUICKLOGIC CORPORATION

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(in thousands, except per share amounts)

	Three Months Ended		Six Months Ended	
	July 1, 2018	July 2, 2017	July 1, 2018	July 2, 2017
Revenue	$3,122	$3,026	$5,886	$6,196
Cost of revenue	1,592	1,646	2,967	3,443
Gross profit	1,530	1,380	2,919	2,753
Operating expenses:				
Research and development	2,366	2,319	5,065	4,746
Selling, general and administrative	2,610	2,614	5,171	5,028
Total operating expenses	4,976	4,933	10,236	9,774
Loss from operations	(3,446)	(3,553)	(7,317)	(7,021)
Interest expense	(32)	(21)	(56)	(82)
Interest income and other (expense), net	23	1	9	1
Loss before income taxes	(3,455)	(3,573)	(7,364)	(7,102)
Provision for income taxes	29	34	90	70
Net loss	$(3,484)	$(3,607)	$(7,454)	$(7,172)
Net loss per share:				
Basic and Diluted	$(0.04)	$(0.05)	$(0.09)	$(0.10)
Weighted average shares outstanding:				
Basic and Diluted	85,753	79,799	83,176	74,327

Note: Net loss equals to comprehensive loss for all the period presented.

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

QUICKLOGIC CORPORATION

UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

	Six Months Ended	
	July 1, 2018	July 2, 2017
Cash flows from operating activities:		
Net loss	$(7,454)	$(7,172)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	675	709
Stock-based compensation	911	665
Write-down of inventories	126	104
Write-off of equipment	5	—
Changes in operating assets and liabilities:		
Accounts receivable	(1,266)	(212)
Inventories	(857)	(1,409)
Other assets	(95)	265
Trade payables	263	(846)
Accrued liabilities	172	73
Deferred revenue	—	79
Other long-term liabilities	47	(14)
Net cash used in operating activities	(7,473)	(7,758)
Cash flows from investing activities:		
Capital expenditures for property and equipment	(95)	(48)
Net cash used in investing activities	(95)	(48)
Cash flows from financing activities:		
Payment of capital lease obligations	(236)	(299)
Proceeds from line of credit	12,000	6,000
Payment of line of credit	(12,000)	(6,000)
Proceeds from issuance of common stock	15,855	17,304
Stock issuance costs	(1,638)	(1,771)
Taxes for net issuance of stock awards	(125)	(64)
Net cash provided by financing activities	13,856	15,170
Net increase in cash and cash equivalents	6,288	7,364
Cash and cash equivalents at beginning of period	16,527	14,870
Cash and cash equivalents at end of period	$22,815	$22,234
Supplemental schedule of non-cash investing and financing activities :		
Capital lease obligation to finance capital expenditures	$418	$296
Purchase of equipment included in accounts payable	$-	$208

See accompanying Notes to Unaudited Condensed Consolidated Financial Statements.

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QUICKLOGIC CORPORATION

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1 — The Company and Basis of Presentation

QuickLogic Corporation ("QuickLogic" or "the Company") was founded in 1988 and reincorporated in Delaware in 1999. The Company enables Original Equipment Manufacturers, or OEMs to maximize battery life for highly differentiated, immersive user experiences with Smartphone, Wearable, Hearable, Tablet and Internet-of-Things, or IoT devices. QuickLogic delivers these benefits through industry leading ultra-low power customer programmable System on Chip, or SoC semiconductor solutions, embedded software, and algorithm solutions for always-on voice and sensor processing, and enhanced visual experiences. The Company is a fabless semiconductor provider of comprehensive, flexible sensor processing solutions, ultra-low power display bridges, and ultra-low power Field Programmable Gate Arrays, or FPGAs.

The accompanying interim condensed consolidated financial statements are unaudited. In the opinion of management, these statements have been prepared in accordance with United States generally accepted accounting principles, or U.S. GAAP, and include all adjustments, consisting only of normal recurring adjustments, necessary to provide a fair statement of results for the interim periods presented. The Company recommends that these interim condensed consolidated financial statements be read in conjunction with the Company's Form 10-K for the year ended December 31, 2017, which was filed with the Securities and Exchange Commission, or SEC, on March 9, 2018. Operating results for the three and six-month periods ended July 1, 2018 are not necessarily indicative of the results that may be expected for the full year.

QuickLogic's fiscal year ends on the Sunday closest to December 31 and the fiscal quarters each end on the Sunday closest to the end of each calendar quarter. QuickLogic's second fiscal quarters for 2018 and for 2017 ended on July 1, 2018 and July 2, 2017, respectively.

Liquidity

The Company has financed its operations and capital investments through sales of common stock, capital and leases, and bank lines of credit. As of July 1, 2018, the Company's principal sources of liquidity consisted of cash and cash equivalents of $22.8 million and $6.0 million that is available for draw at the Company's election upon credit approval under its revolving line of credit arrangement with Silicon Valley Bank, which expires on September 24, 2018. The Company has drawn down all of the $6.0 million in currently available credit under its revolving line of credit as of July 1, 2018.

Under its Fourth Amendment to the Third Amended and Restated Loan and Security Agreement with its lender, the Company is required to maintain (i) unrestricted cash or cash equivalents at the Silicon Valley Bank or at any of its affiliates at all times in an amount of at least $6,000,000; and (ii) a ratio of quick assets to the results of (i) current liabilities minus (ii) the current portion of deferred revenue plus (iii) the long-term portion of the obligations of at least 1.40 to 1.00, tested as of the last day of each month. This line of credit provides for committed loan advances of up to $6.0 million, subject to increases at the Company's election of up to $12.0 million. The Company is in compliance with all loan covenants as of the end of the current reporting period.

On May 29, 2018, the Company issued 13.5 million shares of common stock, $0.001 par value and warrants to purchases up to 5.4 million shares of common stock at a combined price of $1.15. The warrants are exercisable any time for a period of 60 months from the date of issuance on May 29, 2018, and are exercisable at a price of $1.38 per share. See Note 7 to the Unaudited Condensed Consolidated Financial Statements for more details. The Company received net proceeds of approximately $13.9 million, after deducting underwriting commissions and other offering-related expenses. The Company expects to use the net proceeds for working capital, to accelerate the development of next generation products and for general corporate purposes. The Company may also use a portion of the net proceeds to acquire and/or license technologies and acquire and/or invest in businesses when the opportunity arises; however, the Company currently has no commitments or agreements and are not involved in any negotiations with respect to any such transactions. The shares were offered pursuant to a shelf registration statement filed on December 9, 2016 with the SEC, as amended on March 15, 2017, which was declared effective by the SEC on March 16, 2017, and as supplemented by a prospectus supplement dated May 25, 2018, which were filed with the SEC pursuant to Rule 424(b) under the Securities Act of 1933, as amended.

The Company currently uses its cash to fund its capital expenditures and operations. Based on past operating performance and current annual operating plans, the Company believes that its existing cash and cash equivalents, together with available financial resources from the revolving line of credit with Silicon Valley Bank, will be sufficient to fund its operations and capital expenditures and provide adequate working capital for the next twelve months from the date the unaudited condensed consolidated financial statements as of and for the six-month period ended July 1, 2018 are available to be issued.

QUICKLOGIC CORPORATION

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

The Company's liquidity is affected by many factors including, among others: the level of revenue and gross profit as a result of the cyclicality of the semiconductor industry; the conversion of design opportunities into revenue; market acceptance of existing and new products, including solutions based on its Sensor Processing solution platforms; fluctuations in revenue as a result of product end-of-life; fluctuations in revenue as a result of the stage in the product life cycle of its customers' products; costs of securing access to and availability of adequate manufacturing capacity; levels of inventories; wafer purchase commitments; customer credit terms; the amount and timing of research and development expenditures; the timing of new product introductions; production volumes; product quality; sales and marketing efforts; the value and liquidity of its investment portfolio; changes in operating assets and liabilities; the ability to obtain or renew debt financing and to remain in compliance with the terms of existing credit facilities; the ability to raise funds from the sale of equity in the Company; the issuance and exercise of stock options and participation in the Company's employee stock purchase plan; and other factors related to the uncertainties of the industry and global economics.

Over the longer term, the Company anticipates that sales generated from its new product offerings, existing cash and cash equivalents, together with financial resources from its revolving line of credit with Silicon Valley Bank and its ability to raise additional capital in the public capital markets will be sufficient to satisfy its operations and capital expenditures for the next twelve months from the date the unaudited condensed consolidated financial statements as of and for the six-month period ended July 1, 2018 are available to be issued. The Company’s revolving line of credit will expire in September 2018 and it would need to renew this line of credit or find an alternative lender prior to the expiration date. Further, any violations of debt covenants during 2018 will restrict our access to any additional cash draws from the revolving line of credit, and may require immediate repayment of the outstanding debt amounts. The Company believes that it will be able to either renew the revolving line of credit or obtain alternative financing on acceptable terms. However, the Company cannot provide any assurance that it will be able to raise additional capital, if required, or that such capital will be available on terms acceptable to the Company. The inability of the Company to generate sufficient sales from its new product offerings and/or raise additional capital if needed could have a material adverse effect on the Company’s operations and financial condition, including its ability to maintain compliance with its lender’s financial covenants.

Principles of Consolidation

The consolidated financial statements include the accounts of QuickLogic and its wholly-owned subsidiaries. All intercompany accounts and transactions have been eliminated.

Foreign Currency

The functional currency of the Company's non-U.S. operations is the U.S. dollar. Accordingly, all monetary assets and liabilities of these foreign operations are translated into U.S. dollars at current period-end exchange rates and non-monetary assets and related elements of expense are translated using historical exchange rates. Income and expense elements are translated to U.S. dollars using the average exchange rates in effect during the period. Gains and losses from the foreign currency transactions of these subsidiaries are recorded as interest income and other expense, net in the unaudited condensed consolidated statements of operations.

Uses of Estimates

The preparation of these 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, the disclosures of contingent assets and liabilities and the reported amounts of revenue and expenses during the period. Actual results could differ materially from those estimates, particularly in relation to revenue recognition, the allowance for doubtful accounts, sales returns, valuation of investments, valuation of long-lived assets including mask sets, valuation of inventories including identification of excess quantities, market value and obsolescence, measurement of stock-based compensation awards, accounting for income taxes and estimating accrued liabilities.

Contracts with customers often include promises to transfer multiple products and services to a customer. Determining whether products and services are considered distinct performance obligations that should be accounted for separately versus together may require significant judgment.

Judgment is required to determine the Stand Alone Selling Price, or SSP, for each distinct performance obligation. The Company uses a range of amounts to estimate SSP when each of the products and services are sold separately and determines the discount to be allocated based on the relative SSP of the various products and services when products and services sold are bundled. In instances where SSP is not directly observable, such as when the Company does not sell the product or service separately, it determines the SSP using information that may include market conditions and other observable inputs. The

QUICKLOGIC CORPORATION

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

Company typically has more than one SSP for individual products and services due to the stratification of those products and services by customers. In these instances, the Company may use information such as the size of the customer, customer tier, type of the technology used, customer demographics, geographic region and other factors in determining the SSP.

Concentration of Risk

The Company's accounts receivable are denominated in U.S. dollars and are derived primarily from sales to customers located in North America, Asia Pacific, and Europe. The Company performs ongoing credit evaluations of its customers and generally does not require collateral. See Note 11 for information regarding concentrations associated with accounts receivable.

Note 2 — Significant Accounting Policies

During the six-month period ended July 1, 2018, there were no changes in the Company's significant accounting policies from its disclosures in the Annual Report on Form 10-K for the year ended December 31, 2017. For a discussion of the significant accounting policies, please see the Annual Report on Form 10-K for the fiscal year ended December 31, 2017, filed with the SEC on March 9, 2018.

Revenue Recognition

The Company adopted Accounting Standards Update, or ASU, No. 2014-09, Revenue from Contracts with Customers (Topic 606) and related ASU 2016-08, ASU 2016-10, ASU 2016-12 and ASU 2016-20, which provide supplementary guidance, and clarifications, effective January 1, 2018. The results for the reporting period beginning after January 1, 2018, are presented in accordance with the new standard, although comparative information for the prior year has not been restated and continues to be reported under the accounting standards and policies in effect for those periods. Adoption of the new standard did not have a significant impact on the current period revenues or on the prior year Consolidated Financial Statements. No transition adjustment was required to the retained earnings of the Company as of January 1, 2018. Under the new standard revenue is recognized as follows:

Revenue is recognized upon transfer of control of promised products or services to customers in an amount that reflects the consideration the Company expects to receive in exchange for those products or services.

The Company determines revenue recognition through the following steps:

- Identification of the contract, or contracts, with a customer
- Identification of the performance obligations in the contract
- Determination of the transaction price
- Allocation of the transaction price to the performance obligations in the contract
- Recognition of revenue when, or as, we satisfy a performance obligation

The Company generates most of its revenue by supplying standard hardware products, which must be programmed before they can be used in an application. The Company also generates revenue from licensing their intellectual property or IP, software tools and royalty from licensing its technology.

Product Revenue

The Company recognizes hardware product revenue at the point of time when control of products is transferred to the customers.

Intellectual Property and Software License Revenue

The Company recognizes IP and Software License revenue at the point of time when the control of IP or software license has been transferred.

QUICKLOGIC CORPORATION

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

Maintenance Revenue

The Company recognizes revenue from maintenance ratably over the term of the underlying maintenance contract term. Renewals of maintenance contracts create new performance obligations that are satisfied over the term with the revenues recognized ratably over the term.

Royalty Revenue

The Company recognizes royalty revenue when the later of the following events occurs:

a) The subsequent sale or usage occurs.

b) The performance obligation to which some or all of the sales-based royalty has been allocated has been satisfied.

Contracts with Multiple Performance Obligations

Some of the IP and Software Licensing contracts with customers contain multiple performance obligations. For these contracts, the Company accounts for individual performance obligations separately if they are distinct. The transaction price is allocated to the separate performance obligations on a relative standalone selling price basis. We determine the standalone selling prices based on our overall pricing objectives, taking into consideration market conditions and other factors, including the value of our contracts, type of the customer, customer tier, type of the technology used, customer demographics, geographic locations, and other factors.

Deferred Revenue

When the Company receives consideration, or such consideration is unconditionally due, prior to transferring goods or services to the customer under the terms of a sales contract, the Company records deferred revenue, which represents a contract liability. The Company recognizes deferred revenue as net sales once control of goods and/or services have been transferred to the customer and all revenue recognition criteria have been met and any constraints have been resolved.

Assets Recognized from Costs to Obtain a Contract with a Customer

The Company recognizes an asset for the incremental costs of obtaining a contract with a customer if it expects the benefit of those costs to be longer than one year.

Practical expedients and exemptions

(i) Taxes collected from customers and remitted to government authorities and that are related to the sales of the Company’s products are excluded from revenues.

(ii) Sales commissions are expensed when incurred because the amortization period would have been one year or less. These costs are recorded in Selling, general and administrative expense in the Condensed Consolidated Statements of Income.

(iii) The Company does not disclose the value of unsatisfied performance obligations for (i) contracts with original expected lengths of one year or less or (ii) contracts for which the Company recognizes revenue at the amount to which it has the right to invoice for the services performed.

New Accounting Pronouncements

Recently adopted accounting pronouncements:

In May 2014, the Financial Accounting Standards Board, or FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606), which supersedes nearly all existing revenue recognition guidance under U.S. GAAP. The core principle of ASU No. 2014-09 is to recognize revenues when promised goods or services are transferred to customers in an amount that reflects the consideration to which an entity expects to be entitled for those goods or services. ASU No. 2014-09 defines a five-step process to achieve this core principle and, in doing so, more judgment and estimates may be required within the revenue recognition process than are required under existing GAAP. In applying this new guidance to contracts within its scope, an entity will: (1) identify the contract(s) with a customer, (2) identify the performance obligation in the contract, (3) determine the transaction price, (4) allocate the transaction price to the performance obligations in the contract, and (5)

QUICKLOGIC CORPORATION

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

recognize revenue when (or as) the entity satisfies a performance obligation. Additionally, this new guidance would require significantly expanded disclosures about revenue. The new standard allows for two transition methods: (i) a full retrospective method applied to each prior reporting period presented, or (ii) a modified retrospective method applied with the cumulative effect of adoption recognized on adoption. ASU 2014-09 is effective for annual reporting periods beginning after December 15, 2017, including interim reporting periods within that reporting period. In March, April, May and December 2016, the FASB issued ASU Nos. 2016-08, 2016-10, 2016-12 and 2016-20, respectively, which provide supplemental guidance and clarification to ASU No. 2014-09.

The Company adopted ASU No. 2014-09 and other supplementary guidance effective January 1, 2018 and applied the modified retrospective approach for the transition. After evaluation of the impact of the transition, the Company determined that this new standard has no impact on the revenues of the prior years and no adjustments are required to the Company's retained earnings as of January 1, 2018.

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments. This update clarifies how certain cash receipts and cash payments are presented and classified in the statement of cash flows. This ASU is effective for public business entities for fiscal years beginning after December 15, 2017, and for interim periods therein with early adoption permitted and must be applied retrospectively to all periods presented. The Company adopted this Accounting Standard effective January 1, 2018. The Company evaluated the impact on the financial statements and determined that the adoption of ASU No. 2016-15 had no impact on the consolidated financial statements.

In October 2016, the FASB issued ASU No. 2016-16, Income Taxes (Topic 740): Intra-Entity transfers of assets other than inventory. This update removes the requirement under which the income tax consequences of intra-entity transfers are deferred until the assets are ultimately sold to an outside party, except for transfers of inventory. The tax consequences of such transfers would be recognized in tax expense when the transfers occur. The standard is effective for annual reporting periods beginning after December 15, 2017, and interim periods within those annual periods. The Company adopted this Accounting Standard effective January 1, 2018 and determined that the adoption of ASU No. 2016-16 had no impact on the consolidated financial statements.

In May 2017, the FASB issued ASU No. 2017-09, Compensation-Stock Compensation (Topic 718). ASU No. 2017-09 provides clarification on when modification accounting should be used for changes to the terms or conditions of a share-based payment award. This ASU does not change the accounting for modifications but clarifies that modification accounting guidance should only be applied if there is a change to the value, vesting conditions or award classification and would not be required if the changes are considered non-substantive. The amendments of this ASU are effective for reporting periods beginning after December 15, 2017. The Company adopted this Accounting Standard effective January 1, 2018. The Company evaluated the impact on the financial statements and determined that the adoption of ASU No. 2017-09 had no impact on the consolidated financial statements.

Recently issued accounting pronouncements not yet adopted:

In February 2016, the FASB issued ASU No. 2016-02, Leases. The new standard establishes a right-of-use or ROU model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. A modified retrospective transition approach is required for lessees for capital and operating leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with certain practical expedients available. The Company is currently evaluating the impact of our pending adoption of the new standard on the consolidated financial statements.

In February 2018, FASB issued ASU No. 2018-02, Income Statement - Reporting comprehensive Income. The new standard provides companies with an option to reclassify stranded tax effects resulting from enactment of the Tax Cuts and Jobs Act, or TCJA, from accumulated other comprehensive income to retained earnings. The guidance will be effective for the Company beginning in the first quarter of 2019 with early adoption permitted, and would be applied either in the period of adoption or retrospectively to each period (or periods) in which the effect of the change in the tax rate as a result of TCJA is recognized. The Company does not expect the adoption of this ASU to have a material impact on its results of operations, financial position and cash flows.

QUICKLOGIC CORPORATION

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

In March 2018, FASB issued ASU No. 2018-05, Income Taxes (Topic 740). The new standard allows to insert the SEC's interpretive guidance from Staff Accounting Bulletin No. 118 into the income tax accounting codification under U.S. GAAP. The ASU permits companies to use provisional amounts for certain income tax effects of the Tax Act during a one-year measurement period. The provisional accounting impacts for the Company may change in future reporting periods until the accounting analysis is finalized, which will occur no later than the first quarter of fiscal 2019. The Company is currently evaluating the impact of our pending adoption of the new standard on the consolidated financial statements.

In June 2018, the FASB issued ASU No. 2018-07, Improvements to nonemployee share-based payment accounting. Currently, share-based payments to nonemployees are accounted for under Subtopic 505-50, which significantly differs from the guidance for share-based payments to employees under Topic 718. This ASU supersedes Subtopic 505-50 by expanding the scope of Topic 718 to include nonemployee awards and generally aligning the accounting for nonemployee awards with the accounting for employee awards. The effective date for public companies is for fiscal years beginning after December 15, 2018, and interim periods within those fiscal years. For all other entities, the effective date is fiscal years beginning after December 15, 2019. The Company is currently evaluating the impact of our pending adoption of the new standard on the consolidated financial statements.

Other new accounting pronouncements are disclosed on the Annual Report on Form 10-K for the fiscal year ended December 31, 2017 filed with the SEC on March 9, 2018.

Note 3 — Net Loss Per Share

Basic loss per share is computed by dividing net loss available to common stockholders by the weighted average number of common shares outstanding during the period. Diluted net loss per share was computed using the weighted average number of common shares outstanding during the period plus potentially dilutive common shares outstanding during the period under the treasury stock method. In computing diluted net loss per share, the weighted average stock price for the period is used in determining the number of shares assumed to be purchased from the exercise of stock options and warrants.

For the three and six month periods ended July 1, 2018 and July 2, 2017, 7.3 million and 6.9 million of common shares associated with equity awards and the estimated number of shares to be purchased under the current offering period of the 2009 Employee Stock Purchase Plan were outstanding, respectively. These shares were not included in the computation of diluted net loss per share as they were considered anti-dilutive due to net loss the Company experienced during these periods. Warrants to purchase up to 5.4 million shares were issued in connection with May 29, 2018 stock offering were also not included in the diluted loss per share calculation of the second quarter and the six months ended July I, 2018 as they were also considered anti-dilutive due to the net loss the Company experienced during these periods.

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

Note 4 — Balance Sheet Components

The following table provides details relating to certain balance sheet line items as of July 1, 2018, and December 31, 2017:

	As of July 1, 2018	December 31, 2017
	(in thousands)	
Inventories:		
Work-in-process	$3,519	$2,894
Finished goods	771	665
	$4,290	$3,559
Other current assets:		
Prepaid expenses	$837	$836
Other	262	161
	$1,099	$997
Property and equipment:		
Equipment	$11,040	$10,996
Software	2,811	3,139
Furniture and fixtures	42	46
Leasehold improvements	683	674
	14,576	14,855
Accumulated depreciation and amortization	(12,786)	(12,480)
	$1,790	$2,375
Accrued liabilities:		
Employee related accruals	$1,187	$1,143
Other	641	510
	$1,828	$1,653

Note 5 — Financing Obligations

The following table provides details relating to the Company’s financing obligations as of July 1, 2018 and December 31, 2017:

	As of July 1,	December 31,

	2018	2017
	(in thousands)	
Debt and capital lease obligations:		
Revolving line of credit	$6,000	$ 6,000
Capital leases	418	654
	6,418	6,654
Less: Current portion of debt and capital lease obligations	(6,303)	(6,299)
Long-term portion of debt and capital lease obligations	$115	$ 355

Revolving Line of credit

On August 31, 2017, the Company entered into a Fourth Amendment to the Third Amended and Restated Loan and Security Agreement with Silicon Valley Bank to extend the line of credit for one year through September 24, 2018 and to modify certain financial covenants. This amendment requires the Company to maintain (i) unrestricted cash or cash equivalents at the Silicon Valley Bank or at any of its affiliates at all times in an amount of at least $6,000,000; and (ii) a ratio of quick assets to the results of (i) current liabilities minus (ii) the current portion of deferred revenue plus (iii) the long-term portion of the obligations of at least 1.40 to 1.00, tested as of the last day of each month. This line of credit provides for committed loan advances of up to $6.0 million, subject to increases at the Company's election of up to $12.0 million. The Company is in compliance with all loan covenants as of the end of the current reporting period. Upon each advance, the Company can elect a

QUICKLOGIC CORPORATION

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

Prime Rate advance, which is the prime rate plus the prime rate margin, or a LIBOR advance, which is LIBOR rate plus the LIBOR rate margin. As of the second quarter ended July 1, 2018, the Company had $6.0 million of revolving debt outstanding with an interest rate of 4.88% per annum.

Capital Leases

In December 2017, the Company leased design software under a three-year capital lease at an imputed interest rate of 6.48% per annum. Terms of the agreement require the Company to make annual payments of approximately $52,000 through December 2019, for a total of $156,000. As of July 1, 2018, $95,000 was outstanding under the capital lease, $46,000 of which was classified as a current liability.

In December 2017, the Company leased design software under a three-year capital lease at an imputed interest rate of 6.30% per annum. Terms of the agreement require the Company to make quarterly payments of approximately $34,000 through November 2019, for a total of $273,000. As of July 1, 2018, $194,000 was outstanding under the capital lease, $127,000 of which was classified as a current liability.

In May 2017, the Company leased design software under a three-year capital lease at an imputed interest rate of 5.48% per annum. Terms of the agreement require the Company to make annual payments of approximately $92,000 through June 2019, for a total of $276,000. As of July 1, 2018, $87,000 was outstanding under the capital lease, all of which was classified as a current liability.

In February 2017, the Company leased design software under a three-year capital lease at an imputed interest rate of 5.57% per annum. Terms of the agreement require the Company to make annual payments of approximately $44,000 through February 2019, for a total of $133,000. As of July 1, 2018, $42,000 was outstanding under the capital lease, all of which was classified as a current liability.

In December 2015, the Company leased design software under a two-year capital lease at an imputed interest rate of 4.88% per annum. Terms of the agreement require the Company to make quarterly payments of approximately $23,000 through November 2017, for a total of $182,000. The lease was paid off in November 2017.

In July 2015, the Company leased design software under a three-year capital lease at an imputed interest rate of 4.91% per annum. Terms of the agreement require the Company to make annual payments of approximately $67,000 through July 2017, for a total of $202,000. The lease was fully paid off in July 2017.

Note 6 — Fair Value Measurements

Money market funds classified within Level 2 because they are not actively traded, have been valued using quoted market prices or alternative pricing sources and models utilizing observable market inputs. The following table presents the Company's financial assets that are measured at fair value on a recurring basis as of July 1, 2018 and December 31, 2017, consistent with the fair value hierarchy provisions of the authoritative guidance (in thousands):

	July 1, 2018		December 31, 2017
	Total	Level 2	Total

		Level 1		Level 3		Level 1	Level 2	Level 3
Assets:								
Money market funds [1]	$23,080	$6,863	$16,217	$ —	$15,635	$7,176	$8,459	$ —
Total assets	$23,080	$6,863	$16,217	$ —	$15,635	$7,176	$8,459	$ —

[1] Money market funds are included in cash and cash equivalents on the accompanying consolidated balance sheets as of July 1, 2018 and December 31, 2017.

Note 7 — Stockholders' Equity

Common Stock and Preferred Stock

As of July 1, 2018, the Company is authorized to issue 200 million shares of common stock and has 10 million shares of authorized but unissued shares of preferred stock. Without any further vote or action by the Company's stockholders, the Board of Directors has the authority to determine the powers, preferences, rights, qualifications, limitations or restrictions granted to or imposed upon any wholly unissued shares of undesignated preferred stock.

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

On April 26, 2017, the Company filed an Amended and Restated Certificate of Incorporation with the Secretary of State of the State of Delaware to increase the number of authorized shares of common stock from 100 million to 200 million. The proposal for the amendment was approved by the Company’s stockholders at its 2017 Annual Meeting of Stockholders held on April 26, 2017.

Issuance of Common Stock

On December 6, 2016, the Company filed a shelf registration statement on Form S-3, as amended on March 15, 2017, under which the Company may, from time to time, sell securities in one or more offerings up to a total dollar amount of $40.0 million. The Company's shelf registration statement was declared effective on March 16, 2017.

Under the shelf registration, on May 29, 2018, the Company issued an aggregate of 13.5 million shares of common stock, $0.001 par value and warrants to purchase up to an aggregate of 5.4 million shares of common stock in a confidentially marketed underwritten offering. The common stock and warrants were issued in units (the “Units”), with each Unit consisting of (i) one share of common stock and (ii) a warrant to purchase 0.40 of a share of common stock, at a price of $1.15 per Unit. The Company received total net proceeds from the offering of $13.9 million, net of underwriting discounts and other offering expenses of $1.6 million.

The warrants are exercisable any time for a period of 60 months from the date of issuance on May 29, 2018, and are exercisable at a price of $1.38 per share. The Company allocated the proceeds between the common stock and the warrants based on the relative fair value of each on the date of issuance. The estimated grant date fair value was $0.57 per warrant and was calculated based on the following assumptions used in the Black-Scholes model: expected term of 5 years, risk-free interest rate of 2.58%, expected volatility of 52.75% and expected dividend of zero.

Under the shelf registration, in March 2017, the Company issued an aggregate of 11.3 million shares of common stock, $0.001 par value, in an underwritten public offering at a price of $1.50 per share. The Company received net proceeds from this offering of approximately $15.2 million, net of underwriter's commission and other offering expenses.

The Company previously issued 2.3 million warrants exercisable for the Company's common stock with a strike price of $2.98 in conjunction with a June 2012 financing. These warrants expired in June 2017.

Note 8 — Employee Stock Plans

2009 Stock Plan

The 2009 Stock Plan, or the 2009 Plan, was amended and restated by the Board of Directors in January 2015, in February 2017 and in March 15, 2018 and approved by the Company's stockholders on April 23, 2015, on April 26, 2017 and on April 25, 2018 to, among other things, reserve an additional 2.5 million, 1.5 million and 4.0 million shares of common stock, respectively, for issuance under the 2009 Plan. As of July 1, 2018, approximately 16.5 million shares were reserved for issuance under the 2009 Plan. On March 15, 2018, Board of directors extended the term of the Stock Plan until March 15, 2028.

Employee Stock Purchase Plan

The 2009 Employee Stock Purchase Plan, or the 2009 ESPP, was adopted in March 2009. The 2009 ESPP was amended by the Board of Directors in January 2015 and in February 2017, and was approved by the Company's stockholders on April 23, 2015 and April 26, 2017, to reserve an additional 1.0 million and 1.5 million shares of common stock, respectively, for issuance under the 2009 ESPP. As of July 1, 2018, approximately 4.8 million shares were reserved for issuance under the 2009 ESPP.

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

Note 9 — Stock-Based Compensation

The stock-based compensation expense included in the Company's consolidated financial statements for the three and six-months ended July 1, 2018 and July 2, 2017 was as follows (in thousands):

	Three Months Ended		Six Months Ended	
	July 1, 2018	July 2, 2017	July 1, 2018	July 2, 2017
Cost of revenue	$35	$20	$69	$53
Research and development	207	134	390	273
Selling, general and administrative	237	193	452	339
Total costs and expenses	$479	$347	$911	$665

No stock-based compensation was capitalized during any period presented above.

No stock options were granted during the three and six month periods ended July 1, 2018 and July 2, 2017. As of July 1, 2018 and July 2, 2017, the fair value of unvested stock options, net of expected forfeitures, was approximately $200,000 and $361,000, respectively. The remaining unrecognized stock-based compensation expense is expected to be recognized over a weighted average period of 2.0 years as of July 1, 2018.

Stock-Based Compensation Award Activity

The following table summarizes the activity in the shares available for grant under the 2009 Plan during the six months ended July 1, 2018:

	Shares Available for Grant (in thousands)
Balance at December 31, 2017	3,899
Authorized	4,000
RSUs granted	(1,229)
RSUs forfeited or expired	136
Options forfeited	50

Balance at July 1, 2018	6,856

Stock Options

The following table summarizes stock options outstanding and stock option activity under the 2009 Plan, and the related weighted average exercise price, for the first six months of 2018:

	Number of Shares (in thousands)	Weighted Average Exercise Price	Weighted Average Remaining Term (in years)	Aggregate Intrinsic Value (in thousands)
Balance outstanding at December 31, 2017	3,558	$ 2.09		
Forfeited or expired	(50)			
Balance outstanding at July 1, 2018	3,508	$ 2.08	3.89	$ 285
Exercisable at July 1, 2018	3,066	$ 2.24	3.29	$ 167
Vested and expected to vest at July 1, 2018	3,430	$ 2.11	3.80	$ 263

The aggregate intrinsic value in the table above represents the total pretax intrinsic value, based on the Company's closing stock price of $1.15 as of the end of the Company's current reporting period, which would have been received by the option holders had all option holders exercised their options as of that date.

The total intrinsic value of options exercised during the six months ended July 1, 2018 and July 2, 2017 was $0 and $97,000, respectively. Total cash received from employees as a result of employee stock option exercises during the six months ended July 1, 2018 and July 2, 2017 was approximately $0 and $70,000, respectively. The Company settles employee stock

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

option exercises with newly issued common shares. In connection with these exercises, there was no tax benefit realized by the Company due to the Company's current loss position. Total stock-based compensation related to stock options was $34,000 and $63,000 for the three months and $72,000 and $125,000 for the six months ended July 1, 2018 and July 2, 2017, respectively.

Restricted Stock Units

The Company grants restricted stock units or RSUs, to employees and board of directors with various vesting terms. RSUs entitle the holder to receive, at no cost, one common share for each RSU as it vests. In general, the Company's policy is to withhold shares in settlement of employee tax withholding obligations upon the vesting of RSUs. The stock-based compensation related to RSUs was $382,000 and $284,000 for three months and $722,000 and $473,000 the six months ended July 1, 2018 and July 2, 2017, respectively. As of July 1, 2018 and July 2, 2017, there was $2.3 million and $1.2 million, respectively, in unrecognized compensation expense related to RSUs. The remaining unrecognized stock-based compensation expense is expected to be recorded over a weighted average period of 2.59 years.

A summary of activity for the Company's RSUs for the six months ended July 1, 2018 and information regarding RSUs outstanding and expected to vest as of July 1, 2018 is as follows:

	RSUs & PRSUs Outstanding	
	Number of Shares (in thousands)	Weighted Average Grant Date Fair Value
Nonvested at December 31, 2017	2,363	$ 1.54
Granted	1,229	1.55
Vested	(365)	1.39
Forfeited	(136)	—
Nonvested at July 1, 2018	3,091	$ 1.56

Employee Stock Purchase Plan

The weighted average estimated fair value, as defined by the amended authoritative guidance, of rights issued pursuant to the Company's 2009 ESPP during the second quarters ended July 1, 2018 and July 2, 2017, was $0.47 and

$0.41 per right, respectively.

As of July 1, 2018, 1.4 million shares remained available for issuance under the 2009 ESPP. For the three and six months ended July 1, 2018, the Company recorded stock-based compensation expense related to the 2009 ESPP of $63,000 and $117,000 respectively.

The fair value of rights issued pursuant to the Company's 2009 ESPP was estimated on the commencement date of each offering period using the following weighted average assumptions:

	Three Months Ended		Six Months Ended	
	July 1, 2018	July 2, 2017	July 1, 2018	July 2, 2017
Expected term (months)	6.00	6.0	6.00	6.00
Risk-free interest rate	2.09 %	1.02 %	2.09 %	1.02 %
Volatility	44.76 %	49.71 %	44.76 %	49.71 %
Dividend yield	—	—	—	—

As of July 1, 2018, the unrecognized stock-based compensation expense relating to the Company's 2009 ESPP was $77,000 and is expected to be recognized over a weighted average period of approximately 4.6 months.

Note 10 — Income Taxes

In the second quarters of 2018 and 2017, the Company recorded a net income tax expense of $29,000 and $34,000, respectively. For the six months ended June 1, 2018 and July 2, 2017, the Company recorded a net income tax expense of $90,000 and $70,000, respectively. The income tax expense for the three and six months ended July 1, 2018 and July 2, 2017 relates to income taxes from the Company's foreign operations, which are cost-plus entities.

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

Based on the available objective evidence, management believes it is more likely than not that the Company's US domestic net deferred tax assets will not be fully realizable. Accordingly, the Company has provided a full valuation allowance against the associated deferred tax assets. The Company will continue to assess the realizability of the deferred tax assets in future periods.

The Company had no unrecognized tax benefits as of July 1, 2018 and December 31, 2017, which would affect the Company's effective tax rate. The accrued interest and penalties related to uncertain tax positions was not significant as of July 1, 2018 and December 31, 2017.

The Company does not anticipate any material changes to its unrecognized tax benefits during the next 12 months.

The Company is subject to U.S. federal income tax as well as income taxes in many U.S. states and foreign jurisdictions in which the Company operates. The U.S. tax years from 1998 forward remain effectively open to examination due to the carryover of unused net operating losses and tax credits.

On December 22, 2017, the Tax Cuts and Jobs Act (the "Tax Act") was signed into legislation. The Tax Act introduced a broad range of tax reform measures that significantly change the federal income tax laws. The provisions of the Tax Act that may have significant impact on the Company include the permanent reduction of the corporate income tax rate from 35% to 21% (effective for tax years including or commencing on January 1, 2018), one-time transition tax on post-1986 foreign unremitted earnings, provision for Global Intangible Low-Taxed Income or GILTI, deduction for Foreign-Derived Intangible Income or FDII, repeal of corporate alternative minimum tax, limitation of various business deductions, modification of the maximum deduction of net operating loss with no carryback but indefinite carryforward provision and the limitation on the deductibility of executive compensation. Many provisions in the Tax Act are generally effective in tax years beginning in 2018.

At December 31, 2017, the Company reflected the provisional income tax effects of the Tax Act under Accounting Standards Codification Topic 740, Income Taxes including a re-measurement of the deferred tax assets based on the revised rates at which they are expected to reverse. There was no tax effect related to the re-measurement of U.S. deferred taxes using the relevant tax rate at which the Company expects them to reverse due to the Company having recorded a full valuation allowance against its U.S. federal and state deferred tax assets. The estimated one-time transition tax on post-1986 foreign unremitted earnings should not have a material impact to the effective tax rate as the deemed distribution is offset by taxable losses. The Company continues to appropriately refine such amounts within the measurement period allowed by Staff Accounting Bulletin or SAB No.118, which will be completed no later than the fourth quarter of 2018.

For the six months ended July 1, 2018, the Company noted no additional guidance or information that affects the provisional amounts recorded for the year ended December 31, 2017. The Company will continue to monitor and analyze any additional guidance and information that may be issued by the federal and state tax authorities.

In January 2018, the FASB released guidance on the accounting for tax on the global intangible low-taxed income (“GILTI”) provisions of the Tax Act. The GILTI provisions impose a tax on foreign income in excess of a deemed return on tangible assets of foreign corporations. The Company is not projecting any material impact from GILTI inclusions.

Note 11 — Information Concerning Product Lines, Geographic Information and Revenue Concentration

The Company identifies its business segment based on business activities, management responsibility and geographic location. For all periods presented, the Company operated in a single reportable business segment.

The following is a breakdown of revenue by product line (in thousands):

	Three Months Ended		Six Months Ended	
	July 1, 2018	July 2, 2017	July 1, 2018	July 2, 2017
Revenue by product line [1]:				
New products	$1,581	$1,491	$2,881	$3,403
Mature products	1,541	1,535	3,005	2,793
Total revenue	$3,122	$3,026	$5,886	$6,196

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

(1) For all periods presented: New products include all products manufactured on 180 nanometer or smaller semiconductor processes. eFPGA IP license revenue is also included in new product revenue. Mature products include all products produced on semiconductor processes larger than 180 nanometers.

The following is a breakdown of revenue by shipment destination (in thousands):

	Three Months Ended		Six Months Ended	
	July 1, 2018	July 2, 2017	July 1, 2018	July 2, 2017
Revenue by geography:				
Asia Pacific (1)	$1,372	$1,676	$2,293	$3,409
North America (2)	1,474	1,090	3,039	2,223
Europe	276	260	554	564
Total revenue	$3,122	$3,026	$5,886	$6,196

(1) Asia Pacific includes revenue from Japan of $632,000, or 20% of total revenue, and $370,000, or 12% of total revenue, for the quarters ended July 1, 2018 and July 2, 2017, respectively. For the six months ended July 1, 2018 and July 2, 2017, revenue from Japan was $1.0 million, or 17% of total revenue, and $866,000, or 14%, respectively. Revenue from China was $466,000, or 15% and $356,000, or 12%, for the quarters ended July 1, 2018 and July 2, 2017, respectively. For the six months ended July 1, 2018 and July 2, 2017 revenue from China was $602,000, or 10% and $667,000, or 11%, respectively.

(2) North America includes revenue from the United States of $1.4 million, or 46% of total revenue, and $1.0 million, or 34%, for the quarters ended July 1, 2018 and July 2, 2017, respectively. For the six months ended July 1, 2018 and July 2, 2017, revenue from the United States was $3.0 million, or 50% of total revenue, and $2.2 million, or 35%, respectively.

The following distributors and customers accounted for 10% or more of the Company's revenue for the periods presented:

	Three Months Ended		Six Months Ended	
	July 1, 2018	July 2, 2017	July 1, 2018	July 2, 2017
Distributor "A"	32%	33 %	36%	32 %
Distributor "E"	15%	*	*	*

Distributor "G"	10%	*	*	*
Customer "G"	*	21%	*	22%
Customer "H"	16%	*	13%	*
Customer "J"	15%	*	16%	*
Customer "B"	14%	15%	12%	12%
Customer "I"	10%	*	*	*

The following distributors and customers accounted for 10% or more of the Company's accounts receivable as of the dates presented:

	July 1, 2018	December 31, 2017
Distributor "A"	24%	45%
Distributor “E”	21%	*
Distributor "I"	21%	*
Distributor "G"	14%	*
Customer "G"	*	12%

*Represents less than 10% of accounts receivable as of the date presented.
As of July 1, 2018, less than 10% of the Company's long-lived assets, including property and equipment and other assets, were located outside the United States.

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS -- (Continued)

Note 12 — Commitments and Contingencies

Commitments

The Company's manufacturing suppliers require the forecast of wafer starts several months in advance. The Company is required to take delivery of and pay for a portion of forecasted wafer volume. As of July 1, 2018, and December 31, 2017, the Company had $67,000 and $1.1 million, respectively, of outstanding commitments for the purchase of wafer and finished goods inventory.

The Company has obligations with certain suppliers for the purchase of other goods and services entered into in the ordinary course of business. As of July 1, 2018, total outstanding purchase obligations for other goods and services were $1.6 million, $1.3 million of which are due within the next twelve months.

The Company leases its primary facility under an operating lease that expires in March 2020. In addition, the Company rents development facilities in India as well as sales offices in Europe and Asia. Total rent expense for the three months ended July 1, 2018 and July 2, 2017 was approximately $239,000 and $210,000, respectively. Total rent expense for the first six months of 2018 and 2017 was $477,000 and $421,000, respectively.

Note 13 — Litigation

From time to time, the Company may become involved in legal actions arising in the ordinary course of business including, but not limited to, intellectual property infringement and collection matters. It cannot be assured that any such third party assertions will be resolved: (i) without costly litigation; (ii) in a manner that is not adverse to the Company's financial position, results of operations or cash flows; or (iii) without requiring royalty or other payments which may adversely impact gross profit.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward-Looking Statements

The following Management's Discussion and Analysis of Financial Condition and Results of Operations, as well as information contained in “Risk Factors” in Part II, Item 1A and elsewhere in this Quarterly Report on Form 10-Q, contain “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. We intend that these forward-looking statements be subject to the safe harbor created by those provisions. Forward-looking statements are generally written in the future tense and/or are preceded by words such as “will,” “may,” “should,” “forecast,” “could,” “expect,” “suggest,” “believe,” “antic “intend,” “plan,” "future," "potential," "target," "seek," "continue," "if" or other similar words. Forward-looking statements include statements regarding our strategies as well as (1) our revenue levels, including the commercial success of our solutions and new products, (2) the conversion of our design opportunities into revenue, (3) our liquidity, (4) our gross profit and breakeven revenue level and factors that affect gross profit and the break-even revenue level, (5) our level of operating expenses, (6) our research and development efforts, (7) our partners and suppliers, (8) industry and market trends, (9) our manufacturing and product development strategies and (10) our competitive position.

The following discussion should be read in conjunction with the attached unaudited condensed consolidated financial statements and notes thereto, and with our condensed audited consolidated financial statements and notes thereto for the fiscal year ended December 31, 2017, found in our Annual Report on Form 10-K filed with the Securities and Exchange Commission, or SEC, on March 9, 2018. Although we believe that the assumptions underlying the forward-looking statements contained in this Quarterly Report are reasonable, any of the assumptions could be inaccurate, and therefore there can be no assurance that such statements will be accurate. The risks, uncertainties and assumptions referred to above that could cause our results to differ materially from the results expressed or implied by such forward-looking statements include, but are not limited to, those discussed under the heading “Risk Factors” in Part II, Item 1A hereto and the risks, uncertainties and assumptions discussed from time to time in our other public filings and public announcements. All forward-looking statements included in this document are based on information available to us as of the date hereof. In light of the significant uncertainties inherent in the forward-looking statements included herein, the inclusion of such information should not be regarded as a representation by us or any other person that the results or conditions described in such statements or our objectives and plans will be achieved. Furthermore, past performance in operations and share price is not necessarily indicative of future performance. We disclaim any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise that may arise after the date of this Quarterly Report on Form 10-Q.

Overview

We enable OEMs to maximize battery life for highly differentiated, immersive user experiences with Smartphone, Wearable, Hearable, Tablet and IoT devices. We deliver these benefits through industry leading ultra-low power customer programmable SoC semiconductor solutions, embedded software, and algorithm solutions for always-on voice and sensor processing, and enhanced visual experiences. In addition to delivering our own semiconductor solutions, we have an IP business that licenses our eFPGA technology for use in other semiconductor companies SoCs.

We are also a fabless semiconductor company that designs, markets, and supports primarily silicon solutions, as well as FPGAs, software drivers, associated design software and programming hardware, and eFPGA IP called ArcticPro. Our solutions are created from our new silicon platforms including our EOS™, ArcticLink® III, PolarPro®3, PolarPro II, PolarPro, and Eclipse II products (which together comprise our new product category). Our mature products include primarily pASIC®3 and QuickRAM® as well as programming hardware and design software.

Our semiconductor solutions typically fall into one of three categories: Sensor Processing, Display and Visual Enhancement, and Smart Connectivity. Our solutions include a unique combination of our silicon platforms, IP, custom logic, software drivers, and in some cases, firmware, and application software. All of our silicon platforms are standard devices and must be programmed to be effective in a system. Our IPs range from those that enable always-on context-aware sensor applications, such as our FFE, and our Sensor Manager and Communications Manager technologies, to IP that (i) improves multimedia content, such as our VEE technology, and DPO; and (ii) implements commonly used mobile system interfaces, such as LVDS, MIPI, and SDIO. We provide complete solutions by first architecting the solution jointly with our customer's or ecosystem partner’s engineering group, selecting the appropriate solution platform and IPs, providing custom logic, integrating the logic, programming the device with the IPs and/or firmware, providing software drivers or application software required for the customer's application, and supporting the customer on-site during integration, verification and testing.

We also work with mobile processor manufacturers, sensor manufacturers, and/or voice recognition, sensor fusion and context awareness algorithm developers in the development of reference designs, QVLs, or “Catalog” solutions. Through reference designs that incorporate our solutions, we believe mobile processor manufacturers, sensor manufacturers, and sensor algorithm companies can expand the served available market for their respective products. Furthermore, should a solution development for a processor manufacturer or sensor and/or sensor algorithm company be applicable to a set of common OEMs or ODMs, we can amortize our R&D investment over that set of OEMs/ODMs. We call this type of solution a Catalog solution and we are placing a greater emphasis on developing and marketing these types of solutions.

In order to grow our revenue from its current level, we depend upon increased revenue from our new products, including existing new product platforms, eFPGA IP and platforms currently in development. We expect our business growth to be driven by silicon solutions and eFPGA IP and therefore our solutions revenue growth needs to be strong enough to enable us to sustain profitability while we continue to invest in the development, sales and marketing of our new solution platforms and IPs. The gross margin associated with our solutions is generally lower than the gross margin of our FPGA products, which is primarily due to the price sensitive nature of the higher volume mobile consumer opportunities that we are pursuing with our solutions. The gross margin from our eFPGA IP licensing is generally higher than the gross margins of our semiconductor devices due to the nature of IP having a lower cost of sales.

We continue to seek to expand our revenue, including pursuing high-volume sales opportunities in our target market segments, by providing solutions incorporating our intellectual property, or industry standard interfaces. Our industry is characterized by intense price competition and by lower margins as order volumes increase. While winning large volume sales opportunities will increase our revenue, we believe these opportunities may decrease our gross profit as a percentage of revenue.

During the second quarter of 2018, we generated total revenue of $3.1 million. This represents an increase of 13% from the prior quarter and 3% from the second quarter of 2017. Our new product revenue was $1.6 million, an increase of 22% from the prior quarter and 6% from the second quarter of 2017. Quarter over quarter increase was primarily due to increases in our Display Bridge and Sensor Processing product shipments. Year over year increase was primarily due to an increase in Connectivity product shipments. Our mature product revenue was $1.5 million, which represents an increase of 5% from the prior quarter and flat compared to the second quarter of 2017. We expect our mature product revenue to continue to fluctuate over time.

In second quarter and for the first six months of 2018 and, revenue was generated from diverse customers compared to concentration in one or two customers in the prior quarter and prior years.

We devote substantially all of our development, sales and marketing efforts to our new sensor processing solutions using our EOS™ S3 platforms, derivative products based on software-driven features, development of additional new products and solution platforms, and to our new eFPGA IP licensing initiative. Overall, we reported a net loss of $3.5 million for the second quarter of 2018 compared to a net loss of $3.6 million for the second quarter of 2017.

Critical Accounting Estimates

The methods, estimates and judgments we use in applying our most critical accounting policies have a significant impact on the results we report in our consolidated financial statements. The SEC has defined critical accounting policies as those that are most important to the portrayal of our financial condition and results of operations and require us to make difficult and subjective judgments, often as a result of the need to make estimates of matters that are inherently uncertain. Based on this definition, our critical policies include revenue recognition, valuation of inventories, including identification of excess quantities and product obsolescence, valuation of investments, valuation of long-lived assets, measurement of stock-based compensation and estimation of accrued liabilities. We believe that we apply judgments and estimates in a consistent manner and that this consistent application results in consolidated financial statements and accompanying notes that fairly represent all periods presented. However, any factual errors or errors in these judgments and estimates may have a material impact on our financial statements. During the three and six months ended July1, 2018, there were no changes in our critical accounting policies from our disclosure in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017, filed with the SEC on March 9, 2018 except for the new accounting standards adopted in the first quarter of 2018 as described in Note 2 to the consolidated financial statements. For a discussion of critical accounting policies and estimates, please see Item 7 in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017, filed with the SEC on March 9, 2018. See also Note 2 to the Unaudited Condensed Consolidated Financial Statements as of and for three and six months ended July 1, 2018 for the details of the newly adopted accounting standards.

Results of Operations

The following table sets forth the percentage of revenue for certain items in our condensed consolidated statements of operations for the periods indicated:

	Three Months Ended		Six Months Ended	
	July 1, 2018	July 2, 2017	July 1, 2018	July 2, 2017
Revenue	100 %	100 %	100 %	100 %
Cost of revenue	51 %	54 %	50 %	56 %
Gross profit	49 %	46 %	50 %	44 %
Operating expenses:				
Research and development	76 %	77 %	86 %	77 %
Selling, general and administrative	84 %	86 %	88 %	81 %
Loss from operations	(111)%	(117)%	(124)%	(113)%
Interest expense	(1)%	(1)%	(1)%	(1)%
Interest income and other (expense), net	1 %	— %	— %	— %
Loss before income taxes	(111)%	(118)%	(125)%	(114)%
Provision for income taxes	1 %	1 %	2 %	1 %
Net loss	(112)%	(119)%	(127)%	(115)%

Insignificant percentages are rounded to zero percentage (-%) for disclosure.

Three Months Ended July 1, 2018 and July 2, 2017

Revenue

The table below sets forth the changes in revenue for the three months ended July 1, 2018, as compared to the three months ended July 2, 2017 (in thousands, except percentage data):

	Three Months Ended					
	July 1, 2018		July 2, 2017		Change	
	Amount	% of Total Revenues	Amount	% of Total Revenues	Amount	Percentage
Revenue by product line [1]:						
New products	$1,581	51 %	$1,491	49 %	$90	6 %
Mature products	1,541	49 %	1,535	51 %	6	0 %
Total revenue	$3,122	100 %	$3,026	100 %	$96	3 %

(1) For all periods presented: New products include all products manufactured on 180 nanometer or smaller semiconductor processes. eFPGA IP license revenue is also included in new product revenue. Mature products include all products produced on semiconductor processes larger than 180 nanometers.

The $90,000 increase in new product revenue was primarily due to higher shipments of Connectivity product.

Gross Profit

The table below sets forth the changes in gross profit for the three months ended July 1, 2018 as compared to the three months ended July 2, 2017 (in thousands, except percentage data):

	Three Months Ended					
	July 1, 2018		July 2, 2017		Change	
	Amount	% of Total Revenues	Amount	% of Total Revenues	Amount	Percentage
Revenue	$3,122	100 %	$3,026	100 %	$96	3 %
Cost of revenue	1,592	51 %	1,646	54 %	(54)	(3)%
Gross Profit	$1,530	49 %	$1,380	46 %	$150	11 %

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The $150,000 or 3% increase in gross profit was primarily due to favorable product mix. The sale of previously reserved inventory was $54,000 and $37,000 in the second quarters of 2018 and 2017, respectively.

Our semiconductor products have historically had long product life cycles and obsolescence has not been a significant factor in the valuation of inventories. However, as we continue to pursue opportunities in the mobile market and develop new solutions and products, our product life cycle will be shorter and the risk of obsolescence will increase. In general, our standard manufacturing lead times are longer than the binding forecasts we receive from customers.

Operating Expenses

The table below sets forth the changes in operating expenses for the three months ended July 1, 2018, as compared to the three months ended July 2, 2017 (in thousands, except percentage data):

	Three Months Ended							
	July 1, 2018			July 2, 2017			Change	
	Amount	% of Total Revenues		Amount	% of Total Revenues		Amount	Percentage
R&D expense	$2,366	76	%	$2,319	77	%	$47	2 %
SG&A expense	2,610	84	%	2,614	86	%	(4)	0 %
Total operating expenses	$4,976	160	%	$4,933	163	%	$43	1 %

Research and Development

Our research and development, or R&D, expenses consist primarily of personnel, overhead and other costs associated with SoC software and eFPGA development. The $47,000 increase in R&D expenses in the second quarter of 2018, as compared to the second quarter of 2017, was primarily attributable to costs associated with eFPGA development.

Selling, General and Administrative Expense

Our selling, general and administrative, or SG&A, expenses consist primarily of personnel and related overhead costs for sales, marketing, finance, administration, human resources and general management. SG&A expenses in the second quarter of 2018 was flat compared to the second quarter of 2017.

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

The table below sets forth the changes in interest expense and interest income and other (expense), net for the three months ended July 1, 2018 as compared to the three months ended July 2, 2017 (in thousands, except percentage data):

	Three Months	Change

	Ended July 1, 2018	July 2, 2017	Amount	Percentage
Interest expense	$(32)	$(21)	$(11)	52 %
Interest income and other (expense), net	23	1	$22	2200 %
	$(9)	$(20)	$11	(55)%

We conduct a portion of our research and development activities in India and we have sales and marketing activities in various countries outside of the United States. Most of these international expenses are incurred in local currency. Foreign currency transaction gains and losses are included in net interest and other income (expense), as they occur. We do not use derivative financial instruments to hedge our exposure to fluctuations in foreign currency and, therefore, our results of operations are, and will continue to be, susceptible to fluctuations in foreign exchange gains or losses. Historically, impact of foreign exchange fluctuations on the profit or loss has been immaterial. Interest expense relates primarily to the Company's line of credit facility.

Provision for (benefit from) Income Taxes

The table below sets forth the changes in the provisions for income tax for the three months ended July 1, 2018 as compared to the three months ended July 2, 2017 (in thousands, except percentage data):

	Three Months Ended		Change	
	July 1,	July 2,		
	2018	2017	Amount	Percentage
Provision for income taxes	$ 29	$ 34	$ (5)	-15 %

The income tax provision for the second quarters of 2018 and 2017 were primarily from our foreign subsidiaries, which are cost-plus entities.

As of July 1, 2018, our ability to utilize our tax loss carryforwards in future periods is uncertain, and accordingly, we recorded a full valuation allowance against the U.S. deferred tax assets. We will continue to assess the realizability of deferred tax assets in future periods.

On December 22, 2017, the Tax Cuts and Jobs Act (the "Tax Act") was signed into legislation. The Tax Act introduced a broad range of tax reform measures that significantly change the federal income tax laws. The provisions of the Tax Act that may have significant impact on us include the permanent reduction of the corporate income tax rate from 35% to 21% (effective for tax years including or commencing on January 1, 2018), one-time transition tax on post-1986 foreign unremitted earnings, provision for Global Intangible Low-Taxed Income or GILTI, deduction for Foreign-Derived Intangible Income or FDII, repeal of corporate alternative minimum tax, limitation of various business deductions, modification of the maximum deduction of net operating loss with no carryback but indefinite carryforward provision and the limitation on the deductibility of executive compensation. Many provisions in the Tax Act are generally effective in tax years beginning in 2018.

At December 31, 2017, we reflected the provisional income tax effects of the Tax Act under Accounting Standards Codification Topic 740, Income Taxes, including a re-measurement of the deferred tax assets based on the revised rates at which they are expected to reverse. There was no tax effect related to the re-measurement of U.S. deferred taxes using the relevant tax rate at which we expect them to reverse due to the Company having recorded a full valuation allowance against its U.S. federal and state deferred tax assets. The estimated one-time transition tax on post-1986 foreign unremitted earnings should not have a material impact to the effective tax rate as the deemed distribution is offset by taxable losses. We will continue to appropriately refine such amounts within the measurement period allowed by Staff Accounting Bulletin or SAB No.118, which will be completed no later than the fourth quarter of 2018.

Six Months Ended July 1, 2018 and July 2, 2017

Revenue

The table below sets forth the changes in revenue for the six months ended July 1, 2018, as compared to the six months ended July 2, 2017 (in thousands, except percentage data):

	Six Months Ended July 1, 2018		July 2, 2017		Change	
	Amount	% of Total Revenues	Amount	% of Total Revenues	Amount	Percentage
Revenue by product line [1]:						
New products	$2,881	49 %	$3,403	55 %	$(522)	(15)%
Mature products	3,005	51 %	2,793	45 %	212	8 %
Total revenue	$5,886	100 %	$6,196	100 %	$(310)	(5)%

[1] For all periods presented: New products include all products manufactured on 180 nanometer or smaller semiconductor processes. eFPGA IP license revenue is also included in new product revenue. Mature products include all products produced on semiconductor processes larger than 180 nanometers.

The $522,000 decrease in new product revenue was primarily due to decreased shipment of display bridge product of ArcticLink III and new eFPGA IP license revenue recognized in the first six months of 2018. The $212,000 increase in mature product revenue was primarily due to increased orders from our customers in the aerospace, test and instrumentation sectors. We anticipate that our revenue from tablets and mature products will continue to fluctuate.

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Gross Profit

The table below sets forth the changes in gross profit for the six months ended July 1, 2018, as compared to the six months ended July 2, 2017 (in thousands, except percentage data):

	Six Months Ended July 1, 2018		July 2, 2017		Change	
	Amount	% of Total Revenues	Amount	% of Total Revenues	Amount	Percentage
Revenue	$5,886	100 %	$6,196	100 %	$(310)	(5)%
Cost of revenue	2,967	50 %	3,443	56 %	(476)	(14)%
Gross Profit	$2,919	50 %	$2,753	44 %	$166	6 %

The $166,000, or 6%, increase in gross profit was primarily due to higher matured product revenue in first six months of 2018 compared to the first six months of 2017 and favorable product mix. The sale of previously reserved inventory was $102,000 and $63,000 in the first six months of 2018 and 2017, respectively.

Our semiconductor products have historically had long product life cycles and obsolescence has not been a significant factor in the valuation of inventories. However, as we continue to pursue opportunities in the mobile market and develop new solutions and products, our product life cycle will be shorter and the risk of obsolescence will increase. In general, our standard manufacturing lead times are longer than the binding forecasts we receive from customers

Operating Expenses

The table below sets forth the changes in operating expenses for the six months ended July 1, 2018, as compared to the six months ended July 2, 2017 (in thousands, except percentage data):

	Six Months Ended July 1, 2018		July 2, 2017		Change	
	Amount	% of Total Revenues	Amount	% of Total Revenues	Amount	Percentage
R&D Expense	$5,065	86 %	$4,746	77 %	$319	7 %
SG&A Expense	5,171	88 %	5,028	81 %	$143	3 %
Total Operating Expenses	$10,236	174 %	$9,774	158 %	$462	5 %

Research and development expenses consist primarily of personnel, overhead and other costs associated with, sensor hub and algorithm development, programmable logic design, CSSP design, SOC software and eFPGA development. The $319,000 increase in R&D expenses in the first six months of 2018, as compared to the first six months of 2017 was primarily due to increase of consulting and outside services costs.

Selling, General and Administrative expenses consist primarily of personnel and related overhead costs for sales, marketing, finance, administration, human resources and general management. The $143,000 increase in SG&A expenses in the first six months of 2017, as compared to the first six months of 2017, was primarily due to an increase of compensation-related costs, including stock-based compensation expenses.

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

The table below sets forth the changes in interest expense and interest income and other (expense), net for the six months ended July 1, 2018 as compared to the six months ended July 2, 2017 (in thousands, except percentage data):

	Six Months Ended		Change	
	July 1,	July 2,		
	2018	2017	Amount	Percentage
Interest expense	$(56)	$(82)	$26	(32)%
Interest income and other (expense), net	9	1	8	800%
	$(47)	$(81)	$34	(42)%

We conduct a portion of our research and development activities in India and we have sales and marketing activities in various countries outside of the United States. Most of these international expenses are incurred in local currency. Foreign currency transaction gains and losses are included in net interest and other income (expense), as they occur. We do not use derivative financial instruments to hedge our exposure to fluctuations in foreign currency and, therefore, our results of operations are, and will continue to be, susceptible to fluctuations in foreign exchange gains or losses. Historically, impact of foreign exchange fluctuations on the profit or loss has been immaterial. Interest expense relates primarily to the Company's line of credit facility.

Provision for Income Taxes

The table below sets forth the changes in the income tax provisions for the six months ended July 1, 2018 as compared to the six months ended July 2, 2017 (in thousands, except percentage data):

	Six Months Ended		Change	
	July 1,	July 2,		
	2018	2017	Amount	Percentage
Provision for income taxes	$90	$ 70	$20	29 %

The income tax provisions for the first six months of 2018 and 2017 were primarily from our foreign subsidiaries, which are cost plus entities.

As of July 1, 2018, our ability to utilize our income tax loss carryforwards in future periods is uncertain, and accordingly, we recorded a full valuation allowance against the related U.S. tax provision. We will continue to assess the realizability of deferred tax assets in future periods.

Liquidity and Capital Resources

We have financed our operating losses and capital investments through sales of common stock, capital and operating leases, a revolving line of credit and cash flows from operations. As of July 1, 2018, our principal sources of liquidity consisted of our cash and cash equivalents of $22.8 million and $6.0 million in available credit under our revolving line of credit with Silicon Valley Bank, which matures on September 24, 2018. As of the date hereof, we have drawn down all of the $6.0 million in credit currently available under this revolving line of credit. Additionally, we have an accumulated deficit of approximately $261 million. We have experienced net losses in past years and expect such losses to continue through at least the current fiscal year ending December 30, 2018, as we continue to develop new products, applications and technologies.

On August 31, 2017, the Company entered into a Fourth Amendment to the Third Amended and Restated Loan and Security Agreement with Silicon Valley Bank to extend the line of credit for one year through September 24, 2018 and to modify certain financial covenants. This amendment requires the Company to maintain (i) unrestricted cash or cash equivalents at the Silicon Valley Bank or at any of its affiliates at all times in an amount of at least $6,000,000; and (ii) a ratio of quick assets to the results of (i) current liabilities minus (ii) the current portion of deferred revenue plus (iii) the long-term portion of the obligations of at least 1.40 to 1.00, tested as of the last day of each month. This line of credit provides for committed loan advances of up to $6.0 million, subject to increases at the Company's election of up to $12.0 million. The Company is in compliance with all loan covenants as of the end of the current reporting period.

In May 2018, the Company issued an aggregate of 13,513,510 shares of common stock, $0.001 par value and warrants to purchase up to an aggregate of 5,405,404 shares of common stock in a confidentially marketed underwritten offering. The common stock and warrants were issued in units (the “Units”), with each Unit consisting of (i) one share of common stock and (ii) a warrant to purchase 0.40 of a share of common stock, at a combined price of $1.15 per Unit. The Company received total net proceeds from the offering of $13.9 million, net of underwriting discounts and other offering expenses of $1.6 million.

The warrants are exercisable any time for a period of 60 months from the date of issuance on May 29, 2018, and are exercisable at a price of $1.38 per share. The Company allocated the proceeds between the common stock and the warrants based on the relative fair value of each on the date of issuance. The estimated grant date fair value was $0.57 per warrant and was calculated based on the following assumptions used in the Black-Scholes model: expected term of 5 years, risk-free interest rate of 2.58%, expected volatility of 52.75% and expected dividend of zero.

We received net proceeds of approximately $13.9 million, after deducting underwriting commissions and other offering-related expenses. We use the net proceeds for working capital, to accelerate the development of next generation products and for general corporate purposes. We may also use a portion of the net proceeds to acquire and/or license technologies and acquire and/or invest in businesses when the opportunity arises; however, we currently have no commitments or agreements and are not involved in any negotiations with respect to any such transactions. These shares were offered pursuant to a shelf registration statement filed on December 9, 2016 with the SEC, as amended on March 15, 2017, which was declared effective by the SEC on March 16, 2017, and as supplemented by a prospectus supplement dated May 25, 2018 filed with the SEC pursuant to Rule 424(b) under the Securities Act of 1933, as amended.

As of July 1, 2018, most of our cash and cash equivalents were invested in JP Morgan US Government money market funds rated AAAm/Aaa. As of July 1, 2018, our interest-bearing debt consisted of $418,000 outstanding under capital leases and $6.0 million outstanding under our revolving line of credit.

Cash balances held at our foreign subsidiaries were approximately $513,000 and $950,000 at July 1, 2018 and December 31, 2017, respectively. Earnings from our foreign subsidiaries are currently deemed to be indefinitely reinvested. We do not expect such reinvestment to affect our liquidity and capital resources, and we continually evaluate our liquidity needs and ability to meet global cash requirements as a part of our overall capital deployment strategy. Factors that affect our global capital deployment strategy include anticipated cash flows, the ability to repatriate cash in a tax-efficient manner, funding requirements for operations and investment activities, acquisitions and divestitures and capital market conditions.

In summary, our cash flows were as follows (in thousands):

	Six Months Ended	
	July 1, 2018	July 2, 2017
Net cash used in operating activities	$(7,473)	$(7,758)
Net cash used in investing activities	(95)	(48)
Net cash provided by financing activities	13,856	15,170

Net cash used in operating activities

Net cash used in operating activities was $7.5 million in the first six months of 2018. The cash used in operating activities was a result of the net loss of $7.5 million during this period. Changes in operating assets and liabilities of $1.7 million were offset by an equal amount of non-cash charges of $1.7 million. Non-cash charges consisted primarily of stock-based compensation of $911,000, depreciation and amortization of $675,000, and a write-down of inventory of $126,000. The cash used by changes in operating assets and liabilities was mostly due to an increase of trade receivables of $1.3 million due to timing of shipments, increase of inventory by $857,000 and other assets of $95,000, which was partially offset by an increase of trade payables of $263,000, an increase of accrued liabilities of $172,000 and an increase of other long term liabilities of $47,000.

Net cash used in operating activities was $7.8 million in the first six months of 2017. The cash used in operating activities was a result of the net loss of $7.2 million and changes in operating assets and liabilities of $2.1 million, partially offset by non-cash charges of $1.5 million. Non-cash charges consisted primarily of stock-based compensation of $665,000, depreciation and amortization of $709,000, and a write-down of inventory of $104,000. The cash used by changes in operating assets and liabilities was mostly due to an increase in inventory of $1.4 million to build up new product inventory, an increase in trade receivable of $212,000 due to timing of shipments, decrease of trade payables by $846,000, which was partially offset by an increase of other liabilities and deferred revenue of $152,000, and a decrease of other assets and other long-term liabilities of $265,000 and $14,000, respectively.

Net cash used in investing activities

Net cash used in investing activities in the first six months of 2018 was $95,000, which was primarily due to cash used to pay computer and test equipment associated with software development and production. Capital expenditures, which are largely driven by the development of new products and manufacturing levels, are projected to be approximately $260,000 during the remainder of the 2018 fiscal year.

Net cash used in investing activities in the first six months of 2017 was $48,000, which was primarily due to cash used to pay computer and test equipment associated with the EOS™ S3 hardware and software development and production.

Net cash used in financing activities

Net cash provided by financing activities was $13.9 million in the first six months of 2018, which was primarily derived from the net proceeds related to the issuance of 13.5 million shares of common stock and 5.4 million stock warrants in May 2018 pursuant to a shelf registration statement, and proceeds from the issuance of common stock under our equity plans, which was partially offset by scheduled repayments of $236,000 for lease obligations and tax payments related to net settlement of stock awards of $125,000.

Net cash provided by financing activities was $15.2 million in the first six months of 2017, which was primarily derived from the net proceeds of $15.8 million related to the issuance of 11.3 million shares of common stock in March 2017 pursuant to a shelf registration statement that became effective on March 16, 2017, and proceeds from the issuance of common stock under our equity plans of $305,000, which was partially offset by scheduled repayments of $299,000 for lease obligations and stock issuance expenses accrued in the first quarter, but paid in the second quarter of $529,000.

We currently use our cash to fund capital expenditures and operations. Based on past operating performance and current annual operating plans, we believe that our existing cash and cash equivalents, together with available financial resources from the revolving line of credit facility with Silicon Valley Bank, will be sufficient to fund our operations and capital expenditures, and provide adequate working capital for the next twelve months from the date the unaudited condensed consolidated financial statements as of and for the six-month period ended July 1, 2018 are available to be issued.

Over the longer term, we anticipate that the generation of sales from our new product offerings, existing cash and cash equivalents, together with financial resources from our revolving line of credit with Silicon Valley Bank and our ability to raise additional capital in the public capital markets will be sufficient to satisfy our operations and capital expenditures for the next twelve months from the date the unaudited condensed consolidated financial statements as of and for the six-month period ended July 1, 2018 are available to be issued. Our revolving line of credit will expire in September 2018 and we would need to renew this line of credit or find an alternative lender prior to the expiration date. Further, any violations of debt covenants during 2018 will restrict our access to any additional cash draws from the revolving line of credit, and may require our immediate repayment of the outstanding debt amounts. We believe that we will be able to either renew the revolving line of credit or obtain alternative financing on acceptable terms. We cannot provide any assurance that we will be able to raise additional capital, if required, or that such capital will be available on terms acceptable to us. Our inability to generate sufficient sales from our new product offerings and/or raise additional capital if needed could have a material adverse effect on our operations and financial condition, including our ability to maintain compliance with our lender's financial covenants.

Contractual Obligations and Commercial Commitments

The following table summarizes our contractual obligations and commercial commitments as of July 1, 2018 and the effect such obligations and commitments are expected to have on our liquidity and cash flows in future fiscal periods (in thousands):

	Payments Due by Period		
	Total	Less than 1 Year	1-3 Years
Contractual obligations:			
Operating leases	$1,821	$922	$899
Wafer purchases [1]	67	67	—
Other purchase commitments	1,632	1,343	289
Total contractual cash obligations	$3,520	$2,332	$1,188
Other commercial commitments [2]:			
Revolving line of credit	6,000	6,000	—
Capital lease obligations [3]	418	303	115

Total commercial commitments	6,418	6,303	115
Total contractual obligations and commercial commitments	$9,938	$8,635	$1,303

(1) Certain of our wafer manufacturers require us to forecast wafer starts several months in advance. We are committed to accept the delivery of and pay for a portion of forecasted wafer volume.
(2) Other commercial commitments are included as liabilities on our balance sheet as of July 1, 2018.
(3) For a detailed explanation, see Note 5 to the Unaudited Condensed Consolidated Financial Statements.

Concentration of Suppliers

We depend on a limited number of contract manufacturers, subcontractors, and suppliers for wafer fabrication, assembly, programming and testing, and for the supply of programming equipment. These services are typically provided by one supplier for each of our devices. We generally purchase these single or limited source services through standard purchase orders. Because we rely on independent subcontractors to perform these services, we cannot directly control product delivery schedules, costs or quality levels. Our future success also depends on the financial viability of our independent subcontractors. The decision not to provide these services to us or the inability to supply these services to us, such as in the case of a natural or financial disaster, would have a significant impact on our business. In addition, these subcontracted manufacturers produce

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products for other companies and we must place orders up to several months in advance of expected delivery. Increased demand from other companies could result in these subcontract manufacturers allocating available capacity to customers that are larger or have long-term supply contracts in place and we may be unable to obtain adequate foundry and other capacity at acceptable prices, or we may experience delays or interruption in supply. As a result, we have only a limited ability to react to fluctuations in demand for our products, which could cause us to have an excess or a shortage of inventories of a particular product. Additionally, volatility of economic, market, social and political conditions in countries where these suppliers operate may be unpredictable and could result in a reduction in product revenue or increase our cost of revenue and could adversely affect our business, financial condition and results of operations.

Off-Balance Sheet Arrangements

We do not maintain any off-balance sheet partnerships, arrangements or other relationships with unconsolidated entities or others, often referred to as structured finance or special purpose entities, which are established for the purpose of facilitating off-balance sheet arrangements or other contractually narrow or limited purposes.

Recently Issued Accounting Pronouncements

See Note 2 to the Unaudited Condensed Consolidated Financial Statements for a description of recent accounting pronouncements, including the respective dates of adoption and expected effects on the results of our operations and financial condition.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Interest Rate Risk

Our exposure to market rate risk for changes in interest rates relates primarily to our investment portfolio and variable rate debt. We do not use derivative financial instruments to manage our interest rate risk. We are averse to principal loss and ensure the safety and preservation of invested funds by limiting default, market risk and reinvestment risk. Our investment portfolio is generally comprised of investments that meet high credit quality standards and have active secondary and resale markets. Since these securities are subject to interest rate risk, they could decline in value if interest rates fluctuate or if the liquidity of the investment portfolio were to change. Due to the short duration and conservative nature of our investment portfolio, we do not anticipate any material loss with respect to our investment portfolio. A 10% move in interest rates as of the end of the second quarter of 2018 would have had an immaterial effect on our financial position, results of operations and cash flows.

Foreign Currency Exchange Rate Risk

All of our sales and costs of manufacturing are transacted in U.S. dollars. We conduct a portion of our research and development activities in India and have sales and marketing offices in several locations outside of the United States. We use the U.S. dollar as our functional currency. Most of the costs incurred at these international locations are in local currency. If these local currencies strengthen against the U.S. dollar, our payroll and other local expenses will be higher than we currently anticipate. Since our sales are transacted in U.S. dollars, this negative impact on expenses would not be offset by any positive effect on revenue. Operating expenses denominated in foreign currencies were approximately 27% and 24% of total operating expenses for the first six months of 2018 and 2017, respectively. A currency exchange rate fluctuation of 10% would have caused our operating expenses to change by approximately $278,000 in the first six months of 2018.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Based on management's evaluation as of July 1, 2018, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended) were effective at the reasonable assurance level to ensure that the information required to be disclosed by us in this Quarterly Report on Form 10-Q was (i) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and regulations and (ii) accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

Our management, including our Chief Executive Officer and Chief Financial Officer, does not expect that our disclosure controls and procedures or our internal controls over financial reporting will prevent all errors and frauds. 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.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting that occurred during the period covered by this Quarterly Report on Form 10-Q that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Part II. Other Information

Item 1. Legal Proceedings

See Note 13 of the Unaudited Condensed Consolidated Financial Statements for a description of legal proceedings.

Item 1A. Risk Factors

Our 2017 Annual Report on Form 10-K for the year ended December 31, 2017, filed with the SEC on March 9, 2018, includes a detailed discussion of our risk factors at Part I, Item 1A, Risk Factors, which discussion is hereby incorporated by reference into this Part II, Item 1A.

The risks described in our Annual Report on Form 10-K are not the only risks facing our Company. Additional risks not currently known to us or that we currently deem to be immaterial may also adversely affect our business and results from operations.

Item 6. Exhibits

a. Exhibits

The following Exhibits are filed or incorporated by reference into this report:

Exhibit Number	Description
4.1[(1)]	Form of Warrant
4.2[(1)]	Form of Side Letter
31.1	Certification of Brian C. Faith, Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Suping (Sue) Cheung, Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Brian C. Faith, Chief Executive Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Suping (Sue) Cheung, Chief Financial Officer, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

(1) Incorporated by reference to QuickLogic's Current Report on Form 8-K (Item 1.01) filed on May 29, 2018.

Signatures

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

		QUICKLOGIC CORPORATION
		/s/ Suping (Sue) Cheung
Date:	August 10, 2018	Suping (Sue) Cheung
		Chief Financial Officer
		(as Principal Accounting and Financial Officer and on behalf of the Registrant)

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