
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended: July 3, 2022

☐ **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: 001-40345



SkyWater Technology, Inc.

(Exact name of registrant as specified in its charter)

Delaware

**(State or other jurisdiction of
incorporation or organization)**

37-1839853

**(I.R.S. Employer
Identification No.)**

2401 East 86th Street, Bloomington, Minnesota 55425

(Address of registrant's principal executive offices and zip code)

Registrant's telephone number, including area code: (952) 851-5200

Securities registered under Section 12(b) of the Exchange Act:

Title of Each Class	Trading Symbol	Name of Each Exchange on Which Registered
Common stock, par value \$0.01 per share	SKYT	The Nasdaq Stock Market LLC

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. ☒ Yes ☐ No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 ☐ 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 emerging growth company. See the definitions of “large accelerated filer,” “accelerated filer,” “smaller reporting company” and “emerging growth company” in Rule 12b-2 of the Exchange Act.:

Large accelerated filer ☐

Accelerated filer ☐

Non-accelerated filer ☒

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 17(a)(2)(B) of the Securities Act. ☐

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

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of the latest practicable date:

On August 8, 2022, the number of shares of common stock, \$0.01 par value, outstanding was 40,454,685.

SkyWater Technology, Inc.

TABLE OF CONTENTS

	<u>Page No.</u>
Forward-Looking Statements	3
PART I. FINANCIAL INFORMATION	4
Item 1. Condensed Financial Statements (unaudited)	4
Condensed Consolidated Balance Sheets	4
Condensed Consolidated Statements of Operations	5
Condensed Consolidated Statements of Shareholders' Equity (Deficit)	7
Condensed Consolidated Statements of Cash Flows	8
Notes to Condensed Consolidated Financial Statements	10
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	27
Item 3. Quantitative and Qualitative Disclosures About Market Risk	38
Item 4. Controls and Procedures	38
PART II. OTHER INFORMATION	39
Item 1. Legal Proceedings	39
Item 1A. Risk Factors	40
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds	40
Item 3. Defaults Upon Senior Securities	40
Item 4. Mine Safety Disclosures	40
Item 5. Other Information	40
Item 6. Exhibits	40

FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains statements that we believe to be “forward-looking statements” within the meaning of the Private Securities Litigation Reform Act of 1995. All statements other than statements of historical fact included in this Quarterly Report on Form 10-Q, including, without limitation, our expectations regarding our business, results of operations, financial condition and prospects, are forward-looking statements. When used in this Quarterly Report on Form 10-Q, words such as “may,” “expect,” “anticipate,” “estimate,” “intend,” “plan,” “target,” “seek,” “potential,” “believe,” “will,” “could,” “should,” “would” and “project” or the negative thereof or variations thereon or similar words or expressions that convey the uncertainty of future events or outcomes are generally intended to identify forward-looking statements.

Our forward-looking statements are subject to a number of risks, uncertainties and assumptions. Key factors that may affect our results include, among others, the following:

- our goals and strategies;
- our future business development, financial condition and results of operations;
- our ability to continue operating our sole semiconductor foundry at full capacity;
- our ability to appropriately respond to changing technologies on a timely and cost-effective basis;
- our customer relationships and our ability to retain and expand our customer relationships;
- our ability to accurately predict our future revenues for the purpose of appropriately budgeting and adjusting our expenses;
- our expectations regarding dependence on our largest customers;
- our ability to diversify our customer base and develop relationships in new markets;
- the performance and reliability of our third-party suppliers and manufacturers;
- our ability to procure tools, materials, and chemicals amid industry-wide supply chain shortages;
- our ability to control costs, including our operating and capital expenses;
- the size and growth potential of the markets for our solutions, and our ability to serve and expand our presence in those markets;
- the level of demand in our customers’ end markets;
- our ability to attract, train and retain key qualified personnel in a competitive labor market;
- adverse litigation judgments, settlements or other litigation-related costs;
- changes in trade policies, including the imposition of tariffs;
- our ability to raise additional capital or financing;
- our ability to accurately forecast demand;
- the impact of the coronavirus 2019, or COVID-19, pandemic on our business, results of operations and financial condition and our customers, suppliers and workforce;
- the impact of the COVID-19 pandemic on the global economy;
- the level and timing of US government program funding;
- our ability to maintain compliance with certain US government contracting requirements;
- regulatory developments in the United States and foreign countries;
- our ability to protect our intellectual property rights; and
- other factors disclosed in the section entitled “Risk Factors” and elsewhere in our Annual Report on Form 10-K for the year ended January 2, 2022.

Moreover, our business, results of operations, financial condition and prospects may be affected by new risks that could emerge from time to time. In light of these risks, uncertainties and assumptions, the forward-looking events and outcomes discussed in this Quarterly Report on Form 10-Q may not occur and our actual results could differ materially and adversely from those expressed or implied in our forward-looking statements. No forward-looking statement is a guarantee of future performance. You should not rely on forward-looking statements as predictions of future events or outcomes. Although we believe that the expectations reflected in the forward-looking statements are reasonable, the results, levels of activity, performance or events and circumstances reflected in the forward-looking statements may not be achieved or occur.

The forward-looking statements in this Quarterly Report on Form 10-Q represent our views only as of the date hereof. We anticipate that subsequent events and developments will cause our views to change. However, we undertake no obligation to update publicly any forward-looking statements to conform such statements to changes in our expectations or to our actual results, or for any other reason, except as required by law. You should therefore not rely on these forward-looking statements as representing our views as of any date subsequent to the date hereof.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

SKYWATER TECHNOLOGY, INC. Condensed Consolidated Balance Sheets (Unaudited)

	July 3, 2022	January 2, 2022
	(in thousands, except share data)	
Assets		
Current assets:		
Cash and cash equivalents	\$ 10,974	\$ 12,917
Accounts receivable, net	49,906	39,381
Inventories	11,866	17,500
Prepaid expenses and other current assets	6,077	3,854
Income tax receivable	744	745
Total current assets	79,567	74,397
Property and equipment, net	187,141	180,475
Intangible assets, net	6,576	3,891
Other assets	3,363	4,835
Total assets	<u>\$ 276,647</u>	<u>\$ 263,598</u>
Liabilities and Shareholders' Equity		
Current liabilities:		
Current portion of long-term debt	\$ 1,042	\$ 1,021
Accounts payable	13,848	7,637
Accrued expenses	25,094	17,483
Current portion of contingent consideration	441	816
Deferred revenue - current	24,339	20,808
Total current liabilities	64,764	47,765
Long-term liabilities:		
Long-term debt, less current portion and unamortized debt issuance costs	77,190	58,428
Long-term incentive plan	3,636	4,039
Deferred revenue - long-term	79,392	88,094
Deferred income tax liability, net	858	995
Other long-term liabilities	13,178	4,350
Total long-term liabilities	174,254	155,906
Total liabilities	239,018	203,671
Commitments and contingencies		
Shareholders' equity:		
Preferred stock, \$0.01 par value per share (80,000,000 shares authorized; zero issued and outstanding)	—	—
Common stock, \$0.01 par value per share (200,000,000 shares authorized; 40,449,776 and 39,836,038 shares issued and outstanding)	404	398
Additional paid-in capital	121,697	115,208
Accumulated deficit	(84,090)	(54,479)
Total shareholders' equity, SkyWater Technology, Inc.	38,011	61,127
Non-controlling interests	(382)	(1,200)
Total shareholders' equity	37,629	59,927
Total liabilities and shareholders' equity	<u>\$ 276,647</u>	<u>\$ 263,598</u>

The accompanying notes are an integral part of these condensed consolidated financial statements.

SKYWATER TECHNOLOGY, INC.
Condensed Consolidated Statements of Operations
(Unaudited)

	Three Months Ended		Six Months Ended	
	July 3, 2022	July 4, 2021	July 3, 2022	July 4, 2021
(in thousands, except share, unit and per share and unit data)				
Revenue	\$ 47,407	\$ 41,189	\$ 95,528	\$ 89,290
Cost of revenue	45,327	39,377	94,388	78,312
Gross profit	2,080	1,812	1,140	10,978
Research and development	2,361	3,339	4,643	5,266
Selling, general and administrative expenses	10,795	15,415	22,485	24,018
Change in fair value of contingent consideration	—	(942)	—	(886)
Operating loss	(11,076)	(16,000)	(25,988)	(17,420)
Other (expense) income:				
Paycheck Protection Program loan forgiveness	—	6,453	—	6,453
Interest expense	(1,040)	(912)	(2,069)	(1,970)
Total other (expense) income	(1,040)	5,541	(2,069)	4,483
Loss before income taxes	(12,116)	(10,459)	(28,057)	(12,937)
Income tax expense (benefit)	63	(4,237)	(131)	(4,662)
Net loss	(12,179)	(6,222)	(27,926)	(8,275)
Less: net income attributable to non-controlling interests	826	757	1,685	1,515
Net loss attributable to SkyWater Technology, Inc.	\$ (13,005)	\$ (6,979)	\$ (29,611)	\$ (9,790)
Net loss per share attributable to common shareholders, basic and diluted:	\$ (0.32)	\$ (0.20)	\$ (0.74)	\$ (0.54)
Weighted average shares used in computing net loss per common share, basic and diluted:	40,203,050	34,707,758	40,031,615	18,884,051

The accompanying notes are an integral part of these condensed consolidated financial statements.

SKYWATER TECHNOLOGY, INC.
Condensed Consolidated Statements of Shareholders' Equity (Deficit)
For the Three Months Ended July 3, 2022 and July 4, 2021
(dollars, units and shares in thousands)
(Unaudited)

	Class A Units		Class B Units		Common Units		Preferred Stock		Common Stock		Additional	Retained	Total	Non-	Total
	Units	Amount	Units	Amount	Units	Amount	Shares	Amount	Shares	Amount	Paid-in	Earnings	Shareholders'	controlling	Shareholders'
											Capital	(Accumulated	Equity	Interests	Equity
												Deficit)	(Deficit),		(Deficit)
													SkyWater		
													Technology,		
													Inc.		
Balance at April 4, 2021	—	\$ —	18,000	\$ —	2,106	\$ 3,772	—	\$ —	—	\$ —	\$ —	\$ (6,594)	\$ (2,822)	\$ (1,791)	\$ (4,613)
Corporate Conversion	—	—	(18,000)	—	(2,106)	(3,772)	—	—	31,056	311	3,461	—	—	—	—
Issuance of common stock sold in initial public offering, net of issuance costs	—	—	—	—	—	—	—	—	8,004	80	100,082	—	100,162	—	100,162
Stock-based compensation	—	\$ —	—	\$ —	—	\$ —	—	\$ —	—	\$ —	\$ 6,539	\$ —	\$ 6,539	\$ —	\$ 6,539
Distribution to VIE member	—	\$ —	—	\$ —	—	\$ —	—	\$ —	—	\$ —	\$ —	\$ —	\$ —	\$ (392)	\$ (392)
Balance at Net income (loss)	—	\$ —	—	\$ —	—	\$ —	—	\$ —	—	\$ —	\$ —	\$ (6,979)	\$ (6,979)	\$ 757	\$ (6,222)
Balance at July 4, 2021	—	—	—	—	—	—	—	—	39,060	391	110,082	(13,573)	96,900	(1,426)	95,474
Balance at April 3, 2022	—	\$ —	—	\$ —	—	\$ —	—	\$ —	39,905	\$ 399	\$ 118,873	\$ (71,085)	\$ 48,187	\$ (678)	\$ 47,509
Issuance of common stock pursuant to stock-based compensation awards and ESPP	—	—	—	—	—	—	—	—	545	5	781	—	786	—	786
Stock-based compensation	—	—	—	—	—	—	—	—	—	—	2,043	—	2,043	—	2,043
Distribution to VIE member	—	—	—	—	—	—	—	—	—	—	—	—	—	(530)	(530)
Net income (loss)	—	—	—	—	—	—	—	—	—	—	—	(13,005)	(13,005)	826	(12,179)
Balance at July 3, 2022	—	\$ —	—	\$ —	—	\$ —	—	\$ —	40,450	\$ 404	\$ 121,697	\$ (84,090)	\$ 38,011	\$ (382)	\$ 37,629

The accompanying notes are an integral part of these condensed consolidated financial statements.

SKYWATER TECHNOLOGY, INC.
Condensed Consolidated Statements of Shareholders' Equity (Deficit)
For the Six Months Ended July 3, 2022 and July 4, 2021
(dollars, units and shares in thousands)
(Unaudited)

	Class A Units		Class B Units		Common Units		Preferred Stock		Common Stock		Additional	Retained	Total	Non-	Total
	Units	Amount	Units	Amount	Units	Amount	Shares	Amount	Shares	Amount	Paid-in Capital	Earnings (Accumulated Deficit)	Shareholders' Equity (Deficit), SkyWater Technology, Inc.	controlling Interests	Shareholders' Equity (Deficit)
Balance at January 3, 2021	—	\$ —	18,000	\$ —	2,108	\$ 3,767	—	\$ —	—	\$ —	\$ —	\$ (3,783)	\$ (16)	\$ (1,568)	\$ (1,584)
Unit-based compensation	—	—	—	—	—	5	—	—	—	—	—	—	5	—	5
Other	—	—	—	—	(2)	—	—	—	—	—	—	—	—	—	—
Corporate Conversion	—	—	(18,000)	—	(2,106)	(3,772)	—	—	31,056	311	3,461	—	—	—	—
Issuance of restricted common	—	—	—	—	—	—	—	—	8,004	80	100,082	—	100,162	—	100,162
Stock-based compensation	—	—	—	—	—	—	—	—	—	—	6,539	—	6,539	—	6,539
Distribution to VIE member	—	—	—	—	—	—	—	—	—	—	—	—	—	(1,373)	(1,373)
Net income (loss)	—	—	—	—	—	—	—	—	—	—	—	(9,790)	(9,790)	1,515	(8,275)
Balance at July 4, 2021	—	\$ —	—	\$ —	—	\$ —	—	\$ —	39,060	\$ 391	\$ 110,082	\$ (13,573)	\$ 96,900	\$ (1,426)	\$ 95,474
Balance at January 2, 2022	—	\$ —	—	\$ —	—	\$ —	—	\$ —	39,836	\$ 398	\$ 115,208	\$ (54,479)	\$ 61,127	\$ (1,200)	\$ 59,927
Issuance of common stock pursuant to equity compensation plans	—	—	—	—	—	—	—	—	614	6	1,439	—	1,445	—	1,445
Stock-based compensation	—	—	—	—	—	—	—	—	—	—	5,050	—	5,050	—	5,050
Distribution to VIE member	—	—	—	—	—	—	—	—	—	—	—	—	—	(867)	(867)
Net income (loss)	—	—	—	—	—	—	—	—	—	—	—	(29,611)	(29,611)	1,685	(27,926)
Balance at July 3, 2022	—	\$ —	—	\$ —	—	\$ —	—	\$ —	40,450	\$ 404	\$ 121,697	\$ (84,090)	\$ 38,011	\$ (382)	\$ 37,629

The accompanying notes are an integral part of these condensed consolidated financial statements.

SKYWATER TECHNOLOGY, INC.
Condensed Consolidated Statements of Cash Flows
(Unaudited)

	Six Months Ended	
	July 3, 2022	July 4, 2021
	(in thousands)	
Cash flows from operating activities:		
Net loss	\$ (27,926)	\$ (8,275)
Adjustments to reconcile net loss to net cash flows (used in) provided by operating activities:		
Depreciation and amortization	13,657	13,336
Gain on Paycheck Protection Program loan forgiveness	—	(6,453)
Amortization of debt issuance costs included in interest expense	348	320
Long-term incentive and stock-based compensation	5,334	7,008
Change in fair value of contingent consideration	—	(886)
Cash paid for contingent consideration in excess of initial valuation	(375)	(6,114)
Deferred income taxes	(137)	(5,191)
Non-cash revenue related to customer equipment	—	(2,481)
Changes in operating assets and liabilities:		
Accounts receivable	(1,024)	(3,401)
Inventories	(3,865)	(1,998)
Prepaid expenses and other assets	(751)	5,672
Accounts payable and accrued expenses	6,047	(4,482)
Deferred revenue	(5,170)	(16,695)
Income tax payable and receivable	—	(1,171)
Net cash used in operating activities	(13,862)	(30,811)
Cash flows from investing activities:		
Purchase of software and licenses	(400)	(357)
Purchases of property and equipment	(5,463)	(12,898)
Net cash used in investing activities	(5,863)	(13,255)
Cash flows from financing activities:		
Proceeds from issuance of common stock pursuant to the initial public offering, net of underwriting discounts and commissions	—	104,212
Net proceeds on Revolver	18,946	382
Proceeds from the issuance of common stock pursuant to the employee stock purchase plan and a long term incentive plan	1,128	—
Cash paid for offering costs	—	(1,205)
Cash paid for capital leases	(416)	(288)
Distributions to VIE member	(867)	(1,373)
Cash paid on license technology obligations	(500)	—
Repayment of Financing	(509)	(495)
Net cash provided by financing activities	17,782	101,233
Net change in cash and cash equivalents	(1,943)	57,167
Cash and cash equivalents - beginning of period	12,917	7,436
Cash and cash equivalents - end of period	<u>\$ 10,974</u>	<u>\$ 64,603</u>

The accompanying notes are an integral part of these condensed consolidated financial statements.

SKYWATER TECHNOLOGY, INC.
Condensed Consolidated Statements of Cash Flows
(Unaudited)

	Six Months Ended	
	July 3, 2022	July 4, 2021
	(in thousands)	
Supplemental disclosure of cash flow information:		
Cash paid during the period for:		
Interest	\$ 1,857	\$ 1,635
Income taxes	3	1,701
Noncash investing and financing activity:		
Property and equipment acquired, not yet paid	\$ 6,972	\$ 11,444
Common stock issuance costs incurred, not yet paid	—	662
Equipment acquired through capital lease obligations	9,008	2,603
Intangible assets acquired, not yet paid	2,562	—

The accompanying notes are an integral part of these condensed consolidated financial statements.

SKYWATER TECHNOLOGY, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited in thousands, except share, unit and per share and unit data)

Note 1 Nature of Business

SkyWater Technology, Inc., together with its consolidated subsidiaries (collectively, “we”, “us”, “our”, or “SkyWater”), is a U.S. investor-owned, independent, pure-play technology foundry that offers advanced semiconductor development and manufacturing services from our fabrication facility, or fab, in Minnesota and advanced packaging services from our Florida facility. In our technology as a service model, we leverage a strong foundation of proprietary technology to co-develop process technology intellectual property with our customers that enables disruptive concepts through our Advanced Technology Services for diverse microelectronics (integrated circuits, or ICs) and related micro- and nanotechnology applications. In addition to these differentiated technology development services, we support customers with volume production of ICs for high-growth markets through our Wafer Services.

Emerging Growth Company Status

We are an emerging growth company, as defined in the Jumpstart Our Business Startups Act of 2012.

Corporate Conversion and Initial Public Offering

Effective April 14, 2021, we converted into a Delaware corporation pursuant to a statutory conversion and changed our name to SkyWater Technology, Inc. Previously, we operated as a Delaware limited liability company under the name CMI Acquisition, LLC. As a result of the corporate conversion, the holders of the different series of units of CMI Acquisition, LLC, became holders of common stock and options to purchase common stock of SkyWater Technology, Inc. The number of shares of common stock that holders of Class B preferred units and common units were entitled to receive in the corporate conversion was determined in accordance with a plan of conversion, which was based upon the terms of the CMI Acquisition, LLC operating agreement, and varied depending on which class of Units a holder owned. See Note 8 – *Shareholders' Equity*.

On April 23, 2021, we completed our initial public offering (“IPO”) and issued 8,004,000 shares of common stock. Shares of common stock began trading on the Nasdaq Stock Market on April 21, 2021 under the symbol “SKYT”.

Note 2 Basis of Presentation and Principles of Consolidation

The condensed consolidated financial statements as of July 3, 2022, and for the three and six months ended July 3, 2022 and July 4, 2021, are presented in thousands of U.S. dollars (except share and per share information), are unaudited and have been prepared in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) for interim financial information. Accordingly, they do not include all financial information and disclosures required by U.S. GAAP for complete financial statements. These unaudited interim condensed consolidated financial statements should be read in conjunction with our audited consolidated financial statements and the related notes thereto as of January 2, 2022. The unaudited interim condensed consolidated financial statements have been prepared on the same basis as the audited consolidated financial statements and, in the opinion of management, reflect all adjustments, which include normal recurring adjustments, necessary for the fair presentation of our financial position as of July 3, 2022, our results of operations, shareholders' equity (deficit) and cash flows for the three and six months ended July 3, 2022 and July 4, 2021.

The results of operations for the three and six months ended July 3, 2022 are not necessarily indicative of the results of operations to be expected for the year ending January 1, 2023, or for any other interim period, or for any other future year.

Principles of Consolidation

Our condensed consolidated financial statements include our assets, liabilities, revenues, and expenses, as well as the assets, liabilities, revenues, and expenses of subsidiaries in which we have a controlling financial interest, SkyWater Technology Foundry, Inc. (“SkyWater Technology Foundry”), SkyWater Federal, LLC (“SkyWater Federal”), and SkyWater Florida, Inc. (“SkyWater Florida”), and variable interest entities (“VIE”) for which we are the primary beneficiary. All intercompany accounts and transactions have been eliminated in consolidation.

The condensed consolidated statements of operations, shareholders' equity (deficit) and cash flows are for the three and six months ended July 3, 2022 and July 4, 2021, each of which consisted of 13 weeks.

SKYWATER TECHNOLOGY, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited in thousands, except share, unit and per share and unit data)

Liquidity and Cash Requirements

The accompanying Condensed Consolidated Financial Statements have been prepared on the basis of the realization of assets and the satisfaction of liabilities and commitments in the normal course of business and do not include any adjustments to the recoverability and classifications of recorded assets and liabilities as a result of uncertainties.

For the three and six months ended July 3, 2022, we have incurred losses of \$13,005 and \$29,611, respectively. As of July 3, 2022, we had cash and cash equivalents of \$10,974.

Our ability to execute our operating strategy is dependent on our ability to maintain liquidity and continue to access capital through our Revolver (as defined in Note 6 – *Debt*) and other sources of financing. Our current business plans indicate that we will require additional liquidity to continue our operations for the next 12 months from the issuance of the consolidated financial statements. In response to this, we plan to pursue additional debt and equity financing, and are implementing a plan to reduce operating costs to improve cash flow, which includes a reduction in spending and a delayed increase in personnel, and may require us to decrease our level of investment in new products and technologies, discontinue further expansion of our business, or scale back our existing operations. Additionally, the Company obtained a support letter from Oxbow, an affiliate of our principal stockholder, to provide funding in an amount up to \$12,500, if necessary, to enable the Company to meet its obligations as they become due through at least one year and a day beyond the issuance of these financial statements on August 17, 2022. Management believes that based upon its operational forecasts, cash and cash equivalents on hand, available borrowings on our Revolver, cost reduction measures and the support letter from an affiliate of our principal stockholder, as needed, will provide sufficient liquidity to fund its operations for the next 12 months from the issuance of the condensed consolidated financial statements.

The Company has based this estimate on assumptions that may prove to be wrong, and its operating plan may change as a result of many factors currently unknown to it. To the extent that our current resources and plans to reduce expenses are insufficient to satisfy our cash requirements, we may need to seek additional equity or debt financing. Our ability to do so depends on prevailing economic conditions and other factors, many of which are beyond our control.

Use of Estimates

The preparation of our condensed consolidated financial statements in accordance with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenue and expenses during the reporting period. Management evaluates these estimates and judgments on an ongoing basis and bases its estimates on experience, current and expected future conditions, third-party evaluations and various other assumptions that management believes are reasonable under the circumstances. Actual results could differ from those estimates.

COVID-19

In March 2020, the World Health Organization declared the novel coronavirus 2019 (“COVID-19”) outbreak a global pandemic. The COVID-19 pandemic has spread throughout the United States and the world, with the continued potential for significant impact. Our business has been adversely affected by the effects of the COVID-19 pandemic. We implemented modifications to employee travel and employee work locations, as required in some cases by federal, state and local authorities, which has had a negative impact on employee productivity. Because we have manufacturing operations, we may be vulnerable to an outbreak of a new coronavirus or other contagious diseases. Although we have not experienced a shutdown of our manufacturing facilities, the effects of such an outbreak could include the temporary shutdown of our operations or the operations of our customers, disruptions or restrictions on the ability to ship our products to our customers as well as disruptions that may affect our suppliers. Any disruption of our ability to manufacture or distribute our products, the ability of our suppliers to deliver key components on a timely basis, or our customers’ ability to order and take delivery of our products could have a material adverse effect on our revenue and operating results. The future broader implications of the pandemic remain uncertain and will depend on certain future developments, including the duration, scope and severity of the pandemic, the effectiveness of vaccines and the impact of vaccine mandates on our workforce.

Net Loss Per Share

We calculate basic and diluted net loss per common share in conformity with the two-class method required for companies with participating securities. Our previously outstanding Class B preferred units met the criteria of a participating security as they contained the rights to an 8% “preferred return” on the deemed original equity value of each such Class B

SKYWATER TECHNOLOGY, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited in thousands, except share, unit and per share and unit data)

preferred unit (accrued daily since the date of issuance of each such Class B preferred unit). Under the two-class method, income or losses are allocated between the common shareholders and the Class B preferred unitholders. The two-class method includes an allocation formula that determines income or loss per unit for each class according to preferred dividends and undistributed earnings or losses for the period. Our reported net loss for the six months ended July 4, 2021 is increased by the amount allocated to the Class B preferred units to arrive at the loss allocated to common shareholders for purposes of calculating net loss per share. As a result of our April 2021 corporate conversion and IPO, the number of common shares used to compute net loss per common share for the six months ended July 4, 2021 was retrospectively adjusted to reflect the conversion akin to a split-like situation.

Basic net loss per share is calculated by dividing the net loss by the weighted-average number of shares outstanding during the period, without consideration for potentially dilutive securities. Diluted net loss per share is computed by dividing the net loss by the weighted-average number of shares and potentially dilutive securities outstanding for the period determined using the treasury-stock method. Because we reported a net loss for the three and six months ended July 3, 2022 and July 4, 2021, the number of shares used to calculate diluted net loss per common share is the same as the number of shares used to calculate basic net loss per common share because the potentially dilutive shares would have been anti-dilutive if included in the calculation. At July 3, 2022 and July 4, 2021, there were restricted stock units and stock options totaling 2,526,000 and 3,966,000, respectively, excluded from the computation of diluted weighted-average shares outstanding because their inclusion would have been anti-dilutive.

The following table sets forth the computation of basic and diluted net loss per common share for the three and six months ended July 3, 2022 and July 4, 2021:

	Three Months Ended		Six Months Ended	
	July 3, 2022	July 4, 2021	July 3, 2022	July 4, 2021
	(in thousands, except per share data)		(in thousands, except per share data)	
Numerator:				
Net loss attributable to SkyWater Technology, Inc.	\$ (13,005)	\$ (6,979)	\$ (29,611)	\$ (9,790)
Undistributed preferred return to Class B preferred unitholders	—	(39)	—	(398)
Net loss attributable to common shareholders	\$ (13,005)	\$ (7,018)	\$ (29,611)	\$ (10,188)
Denominator:				
Weighted-average common shares outstanding, basic and diluted (1)	40,203,050	34,707,758	40,031,615	18,884,051
Net loss per common share, basic and diluted	\$ (0.32)	\$ (0.20)	\$ (0.74)	\$ (0.54)

- (1) The weighted-average common shares outstanding for the six months ended July 4, 2021 reflects the retrospective adjustment for the April 14, 2021 corporate conversion of 2,105,936 common units into 3,060,343 shares of common stock.

Operating Segment Information

Operating segments are identified as components of an enterprise about which separate financial information is available for evaluation by the chief operating decision-maker in making decisions regarding resource allocation and assessing performance. We view our operations and manage our business as one operating segment.

Note 3 Summary of Significant Accounting Policies

Our audited consolidated financial statements include an additional discussion of the significant accounting policies and estimates used in the preparation of our condensed consolidated financial statements. There were no material changes to our significant accounting policies and estimates during the three and six months ended July 3, 2022, except with respect to the

SKYWATER TECHNOLOGY, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited in thousands, except share, unit and per share and unit data)

adoption of Financial Accounting Standards Board (“FASB”) Accounting Standards Update (“ASU”) 2016-2, Leases (“Topic 842”).

Recently Issued Accounting Standards

In February 2016, the FASB issued Topic 842. The guidance in this ASU supersedes the leasing guidance in Topic 840, Leases. Under the new guidance, lessees are required to recognize lease assets and lease liabilities 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 statement of operations. The standard is effective for public business entities for fiscal years beginning after December 15, 2018. As an emerging growth company, we adopted the new standard on January 3, 2022 for our year ending January 1, 2023. The adoption of Topic 842 did not have a material impact on our condensed consolidated financial statements as disclosed in Note 15 – *Leases*.

In June 2016, the FASB issued a new credit loss accounting standard, ASU 2016-13, Current Expected Credit Losses (“Topic 326”). This guidance replaces the current allowance for loan and lease loss accounting standard and focuses on estimation of expected losses over the life of the loans instead of relying on incurred losses. The standard is effective for certain public business entities for fiscal years beginning after December 15, 2019. As an emerging growth company, we intend to adopt the new standard on January 2, 2023 for our year ending December 31, 2023. However if we lose our emerging growth company status prior to our intended adoption date, we may be required to adopt the new standard in the year we lose such status. We do not expect adopting Topic 326 will have a material impact on our condensed consolidated financial statements.

Note 4 Revenue

Wafer Services Contract

In March 2022, we signed a new contract with a significant wafer services customer. Under the contract, orders are non-cancellable and we have an enforceable right to complete the orders and to payment for any finished or in-process wafers plus a reasonable margin. The wafers produced for that customer are highly customized and have no alternative use to us. Control of these wafers is deemed to transfer to the customer over time during the fabrication process, using the same measure of progress toward satisfying the promise to deliver the units to the customer. Consequently, the transaction price is recognized as revenue over time based on actual costs incurred in the fabrication process to date relative to total expected costs to produce all wafers beginning in March 2022. The contract terms and pricing is applicable to all in-process and future wafers. We recorded revenue of \$8,230 in the first six months of 2022 to account for recognition of wafer services activities in process at the date the contract was signed.

Disaggregated Revenue

The following table discloses revenue by product type and the timing of recognition of revenue for transfer of goods and services to customers:

	Three Months Ended July 3, 2022			
	Topic 606 Revenue		Lease Revenue	Total Revenue
	Point-in-Time	Over Time		
Wafer Services	\$ 3,519	\$ 14,065	\$ —	\$ 17,584
Advanced Technology Services				
T&M	—	20,000	—	20,000
Fixed Price	—	8,656	—	8,656
Other	—	—	1,167	1,167
Total Advanced Technology Services	—	28,656	1,167	29,823
Total revenue	\$ 3,519	\$ 42,721	\$ 1,167	\$ 47,407

SKYWATER TECHNOLOGY, INC.
Notes to Condensed Consolidated Financial Statements

(unaudited in thousands, except share, unit and per share and unit data)

Three Months Ended July 4, 2021				
	Topic 606 Revenue		Lease Revenue	Total Revenue
	Point-in-Time	Over Time		
Wafer Services	\$ 14,312	\$ —	\$ —	\$ 14,312
Advanced Technology Services				
T&M	—	10,692	—	10,692
Fixed Price	—	15,018	—	15,018
Other	—	—	1,167	1,167
Total Advanced Technology Services	—	25,710	1,167	26,877
Total revenue	\$ 14,312	\$ 25,710	\$ 1,167	\$ 41,189

Six Months Ended July 3, 2022				
	Topic 606 Revenue		Lease Revenue	Total Revenue
	Point-in-Time	Over Time		
Wafer Services	\$ 16,724	\$ 22,406	\$ —	\$ 39,130
Advanced Technology Services				
T&M	—	38,908	—	38,908
Fixed Price	—	15,156	—	15,156
Other	—	—	2,334	2,334
Total Advanced Technology Services	—	54,064	2,334	56,398
Total revenue	\$ 16,724	\$ 76,470	\$ 2,334	\$ 95,528

Six Months Ended July 4, 2021				
	Topic 606 Revenue		Lease Revenue	Total Revenue
	Point-in-Time	Over Time		
Wafer Services	\$ 24,331	\$ —	\$ —	\$ 24,331
Advanced Technology Services				
T&M	—	21,484	—	21,484
Fixed Price	—	41,141	—	41,141
Other	—	—	2,334	2,334
Total Advanced Technology Services	—	62,625	2,334	64,959
Total revenue	\$ 24,331	\$ 62,625	\$ 2,334	\$ 89,290

The following table discloses revenue by country as determined based on customer address:

	Three Months Ended		Six Months Ended	
	July 3, 2022	July 4, 2021	July 3, 2022	July 4, 2021
United States	\$ 38,550	\$ 36,612	\$ 80,908	\$ 80,233
United Kingdom	1,443	2,367	3,224	4,453
Canada	1,864	1,547	3,534	3,156
All others	5,550	663	7,862	1,448
	\$ 47,407	\$ 41,189	\$ 95,528	\$ 89,290

Deferred Contract Costs

We recognized amortization of deferred contract costs in our condensed consolidated statements of operations totaling \$399 and \$426 for the three months ended July 3, 2022 and July 4, 2021, respectively, and \$594 and \$977 for the six months ended July 3, 2022 and July 4, 2021, respectively.

SKYWATER TECHNOLOGY, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited in thousands, except share, unit and per share and unit data)

Contract Assets

Contract assets are \$26,005 and \$16,303 at July 3, 2022 and January 2, 2022, respectively, and are included in accounts receivable, net in our condensed consolidated balance sheets. The contract assets balance at July 3, 2022 includes the impact from the new wafer services contract described above, in which we recorded revenue and contract assets of \$8,230 for in-process wafers.

Contract Liabilities

The contract liabilities and other significant components of deferred revenue are as follows:

	July 3, 2022			January 2, 2022		
	Contract Liabilities	Deferred Lease Revenue	Total Deferred Revenue	Contract Liabilities	Deferred Lease Revenue	Total Deferred Revenue
Current	\$ 19,673	\$ 4,666	\$ 24,339	\$ 16,141	\$ 4,667	\$ 20,808
Long-term	70,448	8,944	79,392	76,816	11,278	88,094
Total	<u>\$ 90,121</u>	<u>\$ 13,610</u>	<u>\$ 103,731</u>	<u>\$ 92,957</u>	<u>\$ 15,945</u>	<u>\$ 108,902</u>

The decrease in contract liabilities from January 2, 2022 to July 3, 2022 was primarily the result of completion of specific performance obligations for our customers. Approximately 8% of our total contract liabilities at January 2, 2022 were recognized in revenue in the first six months of 2022. Approximately 20% of our total contract liabilities at January 3, 2021 were recognized in revenue in the first six months of 2021.

Remaining Performance Obligations

As of July 3, 2022, we had approximately \$88,521 of transaction price allocated to remaining performance obligations that are unsatisfied (or partially satisfied) on contracts with an original expected duration of one year or more, which are primarily related to Advanced Technology Services contracts. We expect to recognize those remaining performance obligations as follows:

Within one year	\$ 18,074
From one to two years	16,483
From two to three years	11,394
After three years	42,570
Total	<u>\$ 88,521</u>

We do not disclose the value of remaining performance obligations for contracts with an original expected duration of one year or less. Further, we do not adjust the promised amount of consideration for the effects of a significant financing component if we expect, at contract inception, that the period between when we transfer a promised good or service to a customer and when the customer pays for that good or service will be one year or less.

Note 5 Balance Sheet Information

Certain significant amounts included in our condensed consolidated balance sheets consist of the following:

	July 3, 2022	January 2, 2022
Accounts receivable, net:		
Trade accounts receivable	\$ 23,901	\$ 23,022
Unbilled revenue (contract assets)	26,005	16,303
Other receivables	—	56
Total accounts receivable, net	<u>\$ 49,906</u>	<u>\$ 39,381</u>

SKYWATER TECHNOLOGY, INC.
Notes to Condensed Consolidated Financial Statements

(unaudited in thousands, except share, unit and per share and unit data)

	July 3, 2022	January 2, 2022
Inventories:		
Raw materials	\$ 3,945	\$ 3,340
Work-in-process	335	7,339
Supplies and spare parts	7,586	6,821
Total inventories—current	11,866	17,500
Supplies and spare parts classified as other assets	2,356	2,388
Total inventories	<u>\$ 14,222</u>	<u>\$ 19,888</u>

	July 3, 2022	January 2, 2022
Prepaid expenses and other current assets:		
Prepaid expenses	\$ 1,881	\$ 1,759
Deferred contract costs	3,680	1,579
Prepaid inventory	516	516
Total prepaid assets and other current assets	<u>\$ 6,077</u>	<u>\$ 3,854</u>

	July 3, 2022	January 2, 2022
Property and equipment, net:		
Land	\$ 5,396	\$ 5,396
Buildings and improvements	87,742	87,156
Machinery and equipment	179,784	143,105
Fixed assets not yet in service	11,288	29,229
Total property and equipment, at cost	284,210	264,886
Less: Accumulated depreciation	(97,069)	(84,411)
Total property and equipment, net	<u>\$ 187,141</u>	<u>\$ 180,475</u>

Depreciation expense was \$6,683 and \$6,400 for the three months ended July 3, 2022 and July 4, 2021, respectively, and \$12,714 and \$12,447 for the six months ended July 3, 2022 and July 4, 2021, respectively. In December 2021, we completed an assessment of the useful lives of our machinery and equipment and adjusted the estimated useful life from seven years to ten years to better reflect the estimated periods during which the assets will remain in service. This change in accounting estimate was effective beginning in December of 2021 on a prospective basis for all machinery and equipment acquired after March 1, 2017, the date in which we became an independent company as part of a divestiture from Cypress. The effect of this change in estimate resulted in a \$445 and \$889 decrease in depreciation expense for the three and six months ended July 3, 2022, respectively.

Intangible assets consist of purchased software and license costs from our acquisition of the business in 2017. Additionally, we have entered into license agreements for third-party software and licensed technology, which also comprise intangible assets. During the six months ended July 3, 2022, we acquired third-party software and licensed technology of \$3,062, which will be amortized over a weighted average estimated life of 9.3 years. Intangible assets are summarized as follows:

	July 3, 2022	January 2, 2022
Intangible assets, net:		
Software and licensed technology	\$ 10,277	\$ 6,625
Customer list	—	1,500
Total intangible assets, at cost	10,277	8,125
Less: Accumulated amortization	(3,701)	(4,234)
Total intangible assets, net	<u>\$ 6,576</u>	<u>\$ 3,891</u>

SKYWATER TECHNOLOGY, INC.
Notes to Condensed Consolidated Financial Statements

(unaudited in thousands, except share, unit and per share and unit data)

For the three months ended July 3, 2022 and July 4, 2021, amortization of the customer list intangible asset charged to operations was \$0 and \$88, respectively, and amortization of software and licensed technology was \$518 and \$366, respectively. For the six months ended July 3, 2022 and July 4, 2021, amortization of the customer list intangible asset charged to operations was \$0 and \$176, respectively, and amortization of software and licensed technology was \$943 and \$713, respectively.

Remaining estimated aggregate annual amortization expense is as follows for the years ending:

	Amortization Expense
Remainder of 2022	\$ 1,058
2023	1,635
2024	909
2025	744
2026	577
Thereafter	1,653
Total	<u>\$ 6,576</u>

	July 3, 2022	January 2, 2022
Other assets:		
Supplies and spare parts	\$ 2,356	\$ 2,388
Deferred contract costs	—	1,760
Operating lease right-of-use assets	163	—
Other assets	844	687
Total other assets	<u>\$ 3,363</u>	<u>\$ 4,835</u>

	July 3, 2022	January 2, 2022
Accrued expenses:		
Accrued compensation	\$ 5,007	\$ 4,557
Licensed technology	2,500	—
Accrued commissions	242	189
Accrued fixed asset expenditures	1,728	861
Accrued royalties	3,355	1,854
Capital lease obligations	1,306	1,192
Accrued inventory	1,467	1,966
Other accrued expenses	9,489	6,864
Total accrued expenses	<u>\$ 25,094</u>	<u>\$ 17,483</u>

Note 6 Debt

The components of debt outstanding at July 3, 2022 and January 2, 2022 are as follows:

	July 3, 2022	January 2, 2022
Revolver	\$ 45,167	\$ 26,223
Financing (by VIE)	37,341	37,850
Unamortized debt issuance costs (1)	(4,276)	(4,624)
Total long-term debt, including current maturities	78,232	59,449
Less: Current portion of long-term debt	(1,042)	(1,021)
Long-term debt, excluding current portion and unamortized debt issuance costs	<u>\$ 77,190</u>	<u>\$ 58,428</u>

SKYWATER TECHNOLOGY, INC.**Notes to Condensed Consolidated Financial Statements**

(unaudited in thousands, except share, unit and per share and unit data)

- (1) Unamortized debt issuance costs as of July 3, 2022 included \$1,286 for the Revolver (as defined below) and \$2,990 for the Financing (as defined below). Unamortized debt issuance costs as of January 2, 2022 included \$1,471 for the Revolver and \$3,153 for the Financing (by VIE).

Revolver

The outstanding balance of our amended and restated revolving credit agreement with Wells Fargo Bank, National Association (the “Revolver”) was \$45,167 as of July 3, 2022 at an interest rate of 4.1%. Our remaining availability under the Revolver was \$17,551 as of July 3, 2022. However, we must maintain availability under the Revolver of at least \$15,000 in order to not have to comply with the leverage ratio and fixed charge coverage ratio financial covenants contained in the Revolver with respect to the fiscal quarters ending on or prior to July 2, 2023. As of July 3, 2022, our unused remaining availability was \$17,551 and we were in compliance with applicable financial covenants of the Revolver and expect to be in compliance with applicable financial covenants over the next twelve months.

Maturities

As of July 3, 2022, the Revolver is due in December 2025. The Financing is repayable in equal monthly installments of \$194 over 10 years, with the balance payable at the maturity date of October 6, 2030. Future principal payments of our Revolver and consolidated VIE’s Financing, excluding unamortized debt issuance costs, are as follows:

Remainder of 2022	\$	515
2023		1,060
2024		1,094
2025		46,305
2026		1,177
Thereafter		32,357
Total	\$	<u>82,508</u>

Note 7 Income Taxes

The effective tax rates for the three and six months ended July 3, 2022 and July 4, 2021 differ from the statutory tax rates due to state income taxes, permanent tax differences, the tax impact of the vesting of restricted stock units and changes in our deferred tax asset valuation allowance. The tax rate in any quarter can be affected positively or negatively by adjustments that are required to be reported in the specific quarter of resolution. The effective income tax rate for the three and six months ended July 3, 2022 was (0.5)% and 0.5%, respectively, and the effective tax rate for the three and six months ended July 4, 2021 was 40.5% and 36.0% respectively. The income tax rate applied to our pre-tax loss was lower for the three and six months ended July 3, 2022 than our statutory tax rate of 21% primarily due to a deferred tax asset valuation allowance. The income tax rate applied to our pre-tax loss was higher for the three and six months ended July 4, 2021 than our statutory tax rate of 21% primarily due to the gain realized as a result of the proceeds received from the paycheck protection loan forgiveness program.

Management regularly evaluates the future realization of deferred tax assets and provides a valuation allowance, if considered necessary, based on such evaluation. As part of the evaluation, management has evaluated taxable income in carryback years, future reversals of taxable temporary differences, feasible tax planning strategies, and future expectations of income. Based upon this analysis, a valuation allowance of \$13,662 was recorded as of July 3, 2022 to reduce our net deferred tax assets to the amount that is more likely than not to be realized. The valuation allowance at January 2, 2022 was \$9,819.

No liability has been recorded for uncertain tax positions. We would accrue, if applicable, income tax related interest and penalties in income tax expense in our condensed consolidated statement of operations. There were no interest and penalties incurred during the three and six months ended July 3, 2022 and July 4, 2021.

Note 8 Shareholders’ Equity*Classes of Equity Units*

SKYWATER TECHNOLOGY, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited in thousands, except share, unit and per share and unit data)

Until our corporate conversion on April 14, 2021, we had three classes of limited liability interests, designated as Class A preferred units, Class B preferred units, and common units (collectively, the “Unit” or “Units”). The Class A preferred units were authorized specifically for issuance upon exercise of warrants, of which none were issued and outstanding. Class A preferred units and common units were non-voting classes, and Class B preferred units are a voting class.

Conversion

On April 14, 2021, we completed a corporate conversion. Pursuant to the certificate of incorporation effected in connection with the corporate conversion, our authorized capital stock consists of 200,000,000 shares of voting common stock, par value \$0.01 per share, and 80,000,000 shares of preferred stock, par value \$0.01 per share. As of July 3, 2022, giving effect to the corporate conversion and our IPO, 40,449,776 shares of common stock were issued and outstanding. No shares of our preferred stock were outstanding. On April 21, 2021, our common stock began trading on the Nasdaq Stock Market under the symbol “SKYT”.

Upon the corporate conversion, all Units were converted into an aggregate of 31,055,743 shares of our common stock. Each Class B preferred unit and common unit was converted into a number of shares of common stock determined by dividing (1) the amount that would have been distributed in respect of each such Unit in accordance with CMI Acquisition, LLC’s operating agreement if all assets of CMI Acquisition, LLC had been sold for a cash amount equal to the pre-offering value of CMI Acquisition, LLC, as such value is determined by CMI Acquisition, LLC’s board of managers based on the fair value of each share of common stock (net of any underwriting discounts, fees and expenses), by (2) such per share fair value. The amounts that would have been distributed for this purpose in respect of Class B preferred units and common units were determined by reference to the terms of CMI Acquisition, LLC’s operating agreement, with different values applicable to each series of Units. Before any distributions were made on common units, distributions were made on each Class B preferred unit in an amount equal to the sum of an 8% “preferred return” on the deemed original equity value of each such Class B preferred unit (accrued daily since the date of issuance of each such Class B preferred unit) plus the amount of such original equity value. Only after those distributions were made, the common units, together with the Class B preferred units, shared in the remainder of the distribution on a pro rata basis. For purposes of the corporate conversion, pre-offering “per share fair value” was determined taking into account an assumed initial public offering price of common stock. Accordingly, the outstanding Units were converted as follows:

- holders of Class B preferred units received an aggregate of 27,995,400 shares of common stock; and
- holders of common units received an aggregate of shares 3,060,343 of common stock.

Initial Public Offering

On April 23, 2021, we completed our IPO and issued 8,004,000 shares of common stock, including the underwriter’s exercise of their right to purchase additional shares, at an initial offering price to the public of \$14.00 per share. We received net proceeds from the IPO of approximately \$100,162 after deducting underwriting discounts and commissions of \$7,844 and offering costs of approximately \$4,050.

Note 9 Share-Based Compensation

2021 Equity Incentive Plan

In connection with our IPO, we adopted the 2021 Equity Incentive Plan (the “2021 Equity Plan”). The 2021 Equity Plan became effective upon the consummation of the IPO. As of July 3, 2022, the 2021 Equity Plan provides for the issuance of up to 5,150,000 shares of common stock to eligible individuals in the form of options, stock appreciation rights, restricted stock, restricted stock units, deferred stock units, unrestricted stock, dividend equivalent rights, other equity-based awards and cash bonus awards. The share reserve of the 2021 Equity Plan will be increased effective the first business day of each calendar year by an amount equal to the lesser of: (i) 150,000 shares of common stock; (ii) three percent (3%) of the shares of common stock outstanding on the final day of the immediately preceding calendar year; and (iii) such smaller number of shares of common stock as determined by the compensation committee.

Stock Options

During the six months ended July 3, 2022, we granted 549,000 stock options, respectively, which vest ratably on each of the first, second, third, and fourth anniversaries of the grant date and expire 10 years from the grant date. During the six months ended July 4, 2021, we granted 343,000 stock options which vest in full on the first anniversary of the grant date and expire 15

SKYWATER TECHNOLOGY, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited in thousands, except share, unit and per share and unit data)

months from the grant date; and granted 744,000 stock options which vest ratably on each of the first, second, third, and fourth anniversaries of the grant date and expire 10 years from the grant date. Share-based compensation expense related to stock option awards was \$410 and \$439 for the three months ended July 3, 2022 and July 4, 2021, respectively, and \$832 and \$444 for the six months ended July 3, 2022 and July 4, 2021, respectively. Actual forfeitures are recognized as they occur.

The fair value of each stock option is estimated on the date of grant using a Black-Scholes option-pricing model that uses assumptions noted in the following table. The risk-free interest rate used in the option valuation model was based on yields available on the grant dates for U.S. Treasury Strips with maturity consistent with the expected life assumption. The expected term of the option represents the period of time that options granted are expected to be outstanding and is based on the Securities and Exchange Commission ("SEC") Simplified Method (midpoint of average vesting time and contractual term). Expected volatility is based on an average of the historical, daily volatility of a peer group of similar companies over a period consistent with the expected life assumption ending on the grant date. We assumed no dividend yield in the valuation of the options granted as we have never declared or paid dividends on our common stock and currently intend to retain earnings for use in operations.

	Six Months Ended July 3, 2022
Expected volatility:	47.2%
Expected term (in years):	6.25
Risk-free interest rate:	1.9%

The following table summarizes our stock option activity during the six months ended July 3, 2022:

	Number of Stock Options (in thousands)	Weighted Average Exercise Price Per Share	Aggregate Intrinsic Value (in thousands)	Weighted-Average Remaining Contractual Life
Balance outstanding as of January 2, 2022	986	\$ 14.29		
Granted	549	\$ 11.24		
Exercised	—	\$ —		
Forfeited or canceled	(99)	\$ 13.25		
Balance outstanding as of July 3, 2022	<u>1,436</u>	\$ 13.22	\$ —	7.03 years
Balance vested and exercisable as of July 3, 2022	<u>435</u>	\$ 14.00	\$ —	5.49 years

The weighted average grant-date fair value of options granted in the six months ended July 3, 2022 was \$5.37. As of July 3, 2022, total unrecognized compensation cost related to stock options was \$4,939 and is expected to be recognized over a weighted average period of approximately 3.21 years.

Restricted Common Stock Units

During the six months ended July 3, 2022, we granted 115,000 restricted common stock units to our directors which vest in full on May 31, 2023. In addition, during the six months ended July 3, 2022, we granted 294,000 restricted common stock units, which vest ratably on each of the first, second and third anniversaries of the grant date. During the six months ended July 4, 2021, we granted 441,000 restricted common stock units to eligible employees and directors which vest in full on the first anniversary of the grant date and granted 205,000 restricted common stock units which vest ratably on each of the first, second and third anniversaries of the grant date. The grantee has no rights as a common stockholder until the common stock related to the restricted common stock units is issued upon vesting of the restricted units.

Share-based compensation expense related to restricted common stock unit awards was \$1,411 and \$6,100 for the three months ended July 3, 2022 and July 4, 2021, respectively, and \$3,791 and \$6,100 for the six months ended July 3, 2022 and July 4, 2021, respectively. Actual forfeitures are recognized as they occur. As of July 3, 2022, total unrecognized compensation cost related to restricted common stock units was \$6,585 and is expected to be recognized over a weighted average period of approximately 1.68 years. The estimated fair value of restricted common stock units is based on the grant date closing price of our common stock for time-based vesting awards. During the six months ended July 3, 2022, 991,000 restricted common stock units vested. No restricted common stock units vested during the six months ended July 4, 2021.

SKYWATER TECHNOLOGY, INC.
Notes to Condensed Consolidated Financial Statements

(unaudited in thousands, except share, unit and per share and unit data)

The following table summarizes our restricted common stock unit activity during the six months ended July 3, 2022:

	Number of Restricted Common Stock Units (in thousands)	Weighted Average Grant Date Fair Value Per Share
Balance outstanding as of January 2, 2022	1,745	\$ 8.34
Granted	409	\$ 9.68
Vested	(991)	\$ 8.51
Forfeited or canceled	(73)	\$ 14.63
Balance outstanding as of July 3, 2022	1,090	\$ 8.18

2021 Employee Stock Purchase Plan

In connection with our IPO, we also adopted the 2021 Employee Stock Purchase Plan (the “2021 ESPP”). A maximum of 707,000 shares of our common stock has been reserved for issuance under the 2021 ESPP. Under the 2021 ESPP, eligible employees may purchase our common stock through payroll deductions at a discount not to exceed 15% of the lower of the fair market values of our common stock as of the beginning or end of each offering period, which may range from 6 to 27 months. Payroll deductions are limited to 15% of the employee’s eligible compensation and a maximum of 2,500 shares of our common stock may be purchased by an employee each offering period. The initial six-month offering period commenced on September 1, 2021 and 79,000 shares were purchased under the 2021 ESPP during the six months ended July 3, 2022. As of July 3, 2022 and January 2, 2022, \$889 and \$937, respectively, was withheld on behalf of employees for future purchases under the 2021 ESPP and recorded as accrued compensation. Share-based compensation expense related to the 2021 ESPP was \$223 for the three months ended July 3, 2022 and \$427 for the six months ended July 3, 2022, respectively. Actual forfeitures are recognized as they occur. As of July 3, 2022, total unrecognized compensation cost related to the 2021 ESPP was \$149 and will be recognized on a straight-line basis over the six-month offering period.

The fair value of the 2021 ESPP is estimated on the date of grant using a Black-Scholes option-pricing model that uses assumptions noted in the following table. The risk-free interest rate used in the option valuation model was based on yields available on the grant dates for U.S. Treasury Strips with maturity consistent with the expected life assumption. Expected volatility is based on an average of the historical, daily volatility of a peer group of similar companies over a period consistent with the expected life assumption ending on the grant date. We assumed no dividend yield in the valuation of the options granted as we have never declared or paid dividends on our common stock and currently intend to retain earnings for use in operations.

	Six Months Ended July 3, 2022
Expected volatility:	47.2%
Expected term (in years):	0.50
Risk-free interest rate:	0.60%
Weighted average grant-date fair value per share	\$3.20

Share-Based Compensation Expense Allocation

Share-based compensation expense was allocated in the condensed consolidated statements of operations as follows:

	Three Months Ended		Six Months Ended	
	July 3, 2022	July 4, 2021	July 3, 2022	July 4, 2021
Cost of revenue	\$ 534	\$ 704	\$ 1,574	\$ 704
Research and development	127	1,480	333	1,480
Selling, general and administrative expenses	1,382	4,355	3,143	4,360
	<u>\$ 2,043</u>	<u>\$ 6,539</u>	<u>\$ 5,050</u>	<u>\$ 6,544</u>

SKYWATER TECHNOLOGY, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited in thousands, except share, unit and per share and unit data)

Note 10 Fair Value Measurements

The FASB defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. To determine fair value, we use a fair value hierarchy categorized into three levels based on inputs used. Generally, the three levels are as follows:

- Level 1 – Quoted prices in active markets for identical assets or liabilities;
- Level 2 – Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities; and
- Level 3 – Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Level 3 inputs are used in the valuation of our contingent consideration obligation. The change in level 3 assets measured at fair value on a recurring basis is summarized as follows:

	Six Months Ended	
	July 3, 2022	July 4, 2021
Beginning balance	\$ 816	\$ 10,900
Payments	(375)	(6,114)
Change in fair value	—	(886)
Ending balance	<u>\$ 441</u>	<u>\$ 3,900</u>

Financial assets and liabilities are classified in their entirety based on the lowest level of input that is significant to the fair value measurement. The carrying values of accounts receivable, accounts payable, accrued liabilities, and other financial working capital items approximate fair values at July 3, 2022 and January 2, 2022 due to the short maturity of these items. The carrying values of our borrowings under our Revolver and Financing approximate their fair values due to the frequency of the floating interest rate resets on these borrowings. The fair value of the Revolver and Financing were determined based on inputs that are classified as Level 2 in the fair value hierarchy.

Our non-financial assets such as property and equipment and intangible assets are recorded at fair value upon acquisition and are remeasured at fair value only if an impairment charge is recognized. As of July 3, 2022 and January 2, 2022, we did not have any assets or liabilities measured at fair value on a non-recurring basis.

Note 11 Commitments and Contingencies

Litigation

From time to time, we are involved in legal proceedings and subject to claims arising in the ordinary course of our business. Although the results of litigation and claims cannot be predicted with certainty, we currently believe that the resolution of these ordinary-course matters will not have a material adverse effect on our business, operating results, financial condition or cash flows. Even if any particular litigation is resolved in a manner that is favorable to our interests, such litigation can have a negative impact on us because of defense and settlement costs, diversion of management resources from our business and other factors.

Capital Expenditures

We have various contracts outstanding with third parties which primarily relate to the completion of a building expansion project to increase manufacturing capacity at our Minnesota facility. We have approximately \$12 million of contractual commitments outstanding as of July 3, 2022 that we expect to be paid in the remainder of 2022, through cash on hand and operating cash flows.

Note 12 Major Customers and Concentration Risk

The following customers accounted for 10% or more of revenue for the three and six months ended July 3, 2022 and July 4, 2021:

SKYWATER TECHNOLOGY, INC.
Notes to Condensed Consolidated Financial Statements
(unaudited in thousands, except share, unit and per share and unit data)

	Three Months Ended		Six Months Ended	
	July 3, 2022	July 4, 2021	July 3, 2022	July 4, 2021
Customer A	21 %	19 %	20 %	28 %
Customer B	28 %	28 %	34 %	23 %
Customer C	*	15 %	*	11 %
	49 %	62 %	54 %	62 %

* Represents less than 10% of revenue.

The loss of a major customer could adversely affect our operating results and financial condition.

Note 13 Related Party Transactions

In August 2022, we entered into an agreement with Oxbow Industries, LLC (“Oxbow”), an affiliate of our principal stockholder, CMI Oxbow Partners, LLC, to provide funding in an amount up to \$12,500, if necessary, to enable the Company to meet its obligations as they become due through October 18, 2022.

Professional Services

Oxbow, an affiliate of our principal stockholder, CMI Oxbow Partners, LLC, provided management and financial consulting services to us prior to our IPO. We incurred management fees to Oxbow of \$0 and \$55 of during the three months ended July 3, 2022 and July 4, 2021, respectively, and \$0 and \$215 for the six months ended July 3, 2022 and July 4, 2021, respectively, which have been expensed and included in general and administrative expenses in our condensed consolidated statements of operations.

A member of our board of directors provided legal and professional services to us prior to our IPO. We incurred fees of \$0 and \$1 for the three months ended July 3, 2022 and July 4, 2021, respectively, and \$0 and \$117 for the six months ended July 3, 2022 and July 4, 2021, respectively, which have been expensed and included in general and administrative expenses in our condensed consolidated statements of operations.

Sale-Leaseback Transaction

On September 29, 2020, we entered into an agreement to sell the land and building representing our primary operating location in Bloomington, Minnesota to an entity (“Oxbow Realty”) controlled by our principal stockholder. We subsequently entered into an agreement to lease the land and building from Oxbow Realty for initial payments of \$394 per month over 20 years. The monthly payments are subject to a 2% increase each year during the term of the lease. We are also required to make certain customary payments constituting "additional rent," including certain monthly reserve, insurance and tax payments, in accordance with the terms of the lease agreement. Future minimum lease commitments to Oxbow Realty as of July 3, 2022 were as follows (such amounts are eliminated from our condensed consolidated financial statements due to the consolidation of Oxbow Realty, see Note 14 – *Variable Interest Entities*):

Remainder of 2022	\$ 2,426
2023	4,932
2024	5,031
2025	5,132
2026	5,234
Thereafter	84,116
Total lease payments	106,871
Less: imputed interest	(79,382)
Total	<u>\$ 27,489</u>

SKYWATER TECHNOLOGY, INC.

Notes to Condensed Consolidated Financial Statements

(unaudited in thousands, except share, unit and per share and unit data)

Note 14 Variable Interest Entities

Oxbow Realty was established for the purpose of holding real estate and facilitating real estate transactions. This included facilitating the purchase of our land and building with proceeds from a bank loan and managing the leaseback of the land and building to us. We determined that Oxbow Realty meets the definition of a VIE under Topic 810, *Consolidation*, because it lacks sufficient equity to finance its activities. We concluded that we are the primary beneficiary of Oxbow Realty as we have the power to direct operation and maintenance decisions during the lease term, which would most significantly affect the VIE's economic performance. As the primary beneficiary, we consolidate the assets, liabilities and results of operations of Oxbow Realty, eliminate any transactions between us and Oxbow Realty, and record a non-controlling interest for the economic interest in Oxbow Realty not owned by us because the owners of our common stock do not legally have rights or obligations to those profits or losses. In addition, the assets of Oxbow Realty can only be used to settle its liabilities, and the creditors of Oxbow Realty do not have recourse to the general credit of SkyWater.

The following table shows the carrying amounts of assets and liabilities of Oxbow Realty that are consolidated by us as of July 3, 2022 and January 2, 2022. The assets and liabilities are presented prior to consolidation, and thus a portion of these assets and liabilities are eliminated in consolidation.

	July 3, 2022	January 2, 2022
Cash and cash equivalents	\$ 282	\$ 475
Prepaid expenses	341	192
Finance receivable	37,549	37,437
Other assets	256	200
Total assets	<u>\$ 38,428</u>	<u>\$ 38,304</u>
Accounts payable	\$ 916	\$ 1,232
Accrued expenses	607	479
Debt	37,287	37,793
Total liabilities	<u>\$ 38,810</u>	<u>\$ 39,504</u>

The following table shows the revenue and expenses of Oxbow Realty that are consolidated by us for the three and six months ended July 3, 2022 and July 4, 2021. We have included these amounts, net of eliminations, in the corresponding tables in the notes to our condensed consolidated financial statements.

	Three Months Ended		Six Months Ended	
	July 3, 2022	July 4, 2021	July 3, 2022	July 4, 2021
Revenue	\$ 1,262	\$ 1,159	\$ 2,522	\$ 2,504
General and administrative expenses	102	66	179	318
Interest expense	334	336	658	671
Total expenses	436	402	837	989
Net income	<u>\$ 826</u>	<u>\$ 757</u>	<u>\$ 1,685</u>	<u>\$ 1,515</u>

Note 15 Leases

On January 3, 2022, we adopted ASU No. 2016-02, *Leases*, and all related amendments using the "Comparatives Under 840 Option" transition approach. Under this transition approach, comparative prior periods, including disclosures, were not restated. We elected the transition package of practical expedients which, among other things, allowed us to carry forward historical lease classification. We chose not to elect the hindsight practical expedient. The adoption of the standard did not have an impact on our condensed consolidated statements of operations and there was no adjustment to our retained earnings. We do not expect the adoption of the new standard to have a material impact on our operating results on an ongoing basis.

The most significant impact of the new leases standard was the recognition of right-of-use assets and lease liabilities for operating leases, while our accounting for finance leases remained substantially unchanged. On January 3, 2022, the adoption of the new standard resulted in the recognition of a right-of-use asset of \$184 and a lease liability of \$184.

SKYWATER TECHNOLOGY, INC.
Notes to Condensed Consolidated Financial Statements

(unaudited in thousands, except share, unit and per share and unit data)

We lease certain property and equipment, such as our headquarters in Minnesota, our office location in Florida and certain production equipment under finance leases. We also lease our manufacturing location in Florida and warehouse space in Minnesota under operating leases. We determine if an arrangement is a lease at inception. Leases with an initial term of 12 months or less are not recorded on the balance sheet. On April 1, 2022, we commenced a finance lease for a new nitrogen generator. The lease has a term of 15 years for total fixed payments of approximately \$14,000.

Right-of-use assets represent our right to use an underlying asset for the lease term and lease liabilities represent our obligation to make lease payments arising from the lease. Operating lease right-of-use assets are recognized at commencement date based on the present value of lease payments over the lease term. For leases that do not provide an implicit rate, we use our incremental borrowing rate based on the information available at commencement date in determining the present value of lease payments. Some of our leases include options to extend the term, which is only included in the lease liability and right-of-use assets calculation when it is reasonably certain we will exercise that option. As of July 3, 2022, the operating lease liability and operating right-of-use assets did not include any lease extension options.

We have lease agreements with lease and non-lease components and have elected to account for these as a single lease component only for equipment leases. Lease expense for operating lease payments is recognized on a straight-line basis over the lease term.

The components of lease expense are as follows:

	Three Months Ended July 3, 2022	Six Months Ended July 3, 2022
Operating lease cost	\$ 13	\$ 26
Finance lease cost:		
Amortization of assets	495	842
Interest on lease liabilities	234	322
Variable lease cost	—	—
Total net lease cost	\$ 742	\$ 1,190

Short-term lease cost amounted to \$70 and \$140 for the three and six months ended July 3, 2022, respectively.

Supplemental cash flow information related to leases are as follows:

	Six Months Ended July 3, 2022
Cash paid for amounts included in the measurement of lease liabilities:	
Operating cash flows used for operating leases	\$ 12
Operating cash flows used for finance leases	234
Financing cash flows used for finance leases	416
Right of use assets obtained in exchange for lease liabilities:	
Operating leases	184
Finance leases	9,126

The weighted average remaining lease term and weighted average discount rates related to leases are as follows:

	July 3, 2022
Weighted average remaining lease term:	
Operating leases	3.5 years
Finance leases	13.4 years
Weighted average discount rate:	
Operating leases	4.8%
Finance leases	8.5%

Supplemental balance sheet information related to leases is as follows:

SKYWATER TECHNOLOGY, INC.
Notes to Condensed Consolidated Financial Statements
(unaudited in thousands, except share, unit and per share and unit data)

Leases	Classification	July 3, 2022
Assets		
Operating lease right-of-use assets	Other assets	\$ 163
Finance lease right-of-use assets	Property and equipment, net	10,630
Total lease right-of-use assets		<u>\$ 10,793</u>
Operating lease liabilities		
Current portion of operating lease liabilities	Accrued expenses	\$ 42
Operating lease liabilities, excluding current portion	Other long-term liabilities	122
Total operating lease liabilities		164
Finance lease liabilities		
Current portion of finance lease liabilities	Accrued expenses	1,306
Finance lease liabilities, excluding current portion	Other long-term liabilities	9,489
Total finance lease liabilities		10,795
Total lease liabilities		<u>\$ 10,959</u>

Future maturities of lease liabilities as of July 3, 2022 are as follows:

Fiscal Year	Operating Leases	Finance Leases	Total
Remainder of 2022	\$ 24	\$ 1,288	\$ 1,312
2023	50	1,458	1,508
2024	51	1,234	1,285
2025	54	1,155	1,209
2026	—	1,157	1,157
Thereafter	—	11,977	11,977
Total lease payments	179	18,269	18,448
Less imputed interest	(15)	(7,474)	(7,489)
Total lease liabilities	<u>\$ 164</u>	<u>\$ 10,795</u>	<u>\$ 10,959</u>

With the exception of the future minimum lease commitments related to our lease of the land and building representing our primary operating location in Bloomington, Minnesota, which are eliminated in consolidation, we had no disclosures in the prior year period related to leases.

SkyWater as the Lessor

In March 2020, we executed a contract with a customer that includes the right to use of a portion of our existing facility to produce wafers using the customer's equipment. The contractual amount that relates to revenue from an operating lease was \$21,000, and is being recognized over the estimated lease term of 4.5 years. The total amount was prepaid by the customer and recorded as deferred revenue. See Note 4 – *Revenue* for additional information on revenue recognition and deferred revenue of the operating lease. The carrying value of the facility space utilized by the lessee was approximately \$27,000, net of accumulated depreciation of \$2,248 and \$1,558 as of July 3, 2022 and January 2, 2022, respectively, and is included in property and equipment on our condensed consolidated balance sheets.

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

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the condensed consolidated financial statements and the related notes included elsewhere in this Quarterly Report on Form 10-Q and our audited consolidated financial statements and related notes, included in our Annual Report on Form 10-K for the year ended January 2, 2022. In addition to historical financial information, the following discussion contains forward-looking statements that reflect our current expectations, estimates and assumptions concerning events and financial trends that may affect our future operating results or financial position. Actual results and the timing of events may differ materially from those discussed or implied in our forward-looking statements due to a number of factors, including those described in the sections entitled "Risk Factors" and "Forward-Looking Statements" herein and elsewhere in our Annual Report on Form 10-K.

We refer to the three-month periods ended July 3, 2022 and July 4, 2021 as the second quarter of 2022 and second quarter of 2021, respectively. Each of these three-month periods includes 13 weeks. All percentage amounts and ratios presented in this management's discussion and analysis were calculated using the underlying data in thousands. Unless otherwise indicated, all changes identified for the current period results represent comparisons to results for the prior corresponding period.

For purposes of this section, the terms "we," "us," "our," and "SkyWater" refer to CMI Acquisition, LLC and its subsidiaries collectively before the corporate conversion discussed below and to SkyWater Technology, Inc. and its subsidiaries collectively after the corporate conversion.

Corporate Conversion and Initial Public Offering

On April 14, 2021, in connection with the IPO of our common stock, CMI Acquisition, LLC filed a certificate of conversion, whereby CMI Acquisition, LLC effected a corporate conversion from a Delaware limited liability company to a Delaware corporation and changed its name to SkyWater Technology, Inc., which we refer to as the corporate conversion. As part of the corporate conversion, holders of Class B preferred units and common units of CMI Acquisition, LLC received shares of our common stock for each unit held immediately prior to the corporate conversion using an approximate one-to-1.56 conversion ratio for Class B preferred units and one-to-1.45 conversion ratio for common units.

On April 23, 2021, we completed our IPO and issued 8,004,000 shares of common stock, including the underwriter's exercise of their right to purchase additional shares, at an initial offering price to the public of \$14.00 per share. Shares of our common stock began trading on the Nasdaq Stock Market on April 21, 2021 under the symbol "SKYT".

We received net proceeds from the IPO of approximately \$100.2 million, after deducting underwriting discounts, commissions and offering costs of approximately \$11.9 million. We estimate that we utilized approximately \$45 million of our IPO proceeds to pay down our revolving credit agreement, approximately \$28 million of our IPO proceeds to fund capital expenditures, and approximately \$27 million of our IPO proceeds to fund our operating activities.

Overview

We are a U.S. investor-owned, independent, pure-play technology foundry that offers advanced semiconductor development and manufacturing services from our fabrication facility, or fab, in Minnesota and advanced packaging services from our Florida facility. In our technology as a service model, we leverage a strong foundation of proprietary technology to co-develop process technology intellectual property ("IP") with our customers that enables disruptive concepts through our Advanced Technology Services for diverse microelectronics (integrated circuits, or ICs) and related micro- and nanotechnology applications. In addition to differentiated technology development services, we support customers with volume production of ICs for high-growth markets through our Wafer Services.

The combination of semiconductor development and manufacturing services we provide our customers is not available to them from a conventional fab. In addition, our status as a publicly-traded, U.S.- based, U.S. investor-owned pure-play technology foundry with DMEA Category 1A accreditation from the U.S. Department of Defense, or DoD, is expected to position us well to provide distinct, competitive advantages to our customers. These advantages include the benefits of enhanced IP security and easy access to a U.S. domestic supply chain. In September 2019, we entered into a contract with the DoD to receive up to \$170 million to expand and upgrade our manufacturing capabilities, specifically to build next-generation rad-hard wafer solutions for the aerospace and defense sector which will have significant benefits for other commercial markets. Our fab expansion supporting this project began operations in October 2020. In January 2021, we entered into an agreement with Osceola County, Florida to take over operation of the Center for NeoVation facility in Kissimmee, Florida to accelerate pure-play advanced packaging services for differentiated technologies.

We primarily focus on serving diversified, high-growth end users in numerous vertical markets, including (1) advanced computation, (2) aerospace and defense, or A&D, (3) automotive and transportation, (4) bio-health, (5) consumer and

(6) industrial/internet of things, or IoT. By housing both development and manufacturing in a single operation, we rapidly and efficiently transition newly-developed processes to high-yielding volume production, eliminating the time it would otherwise take to transfer production to a third-party fab. Through our Advanced Technology Services, we specialize in co-creating with our customers advanced solutions that directly serve our end markets, such as superconducting ICs for quantum computing, integrated photonics, carbon nanotube technologies, or CNTs, microelectromechanical systems, or MEMS, technologies for biomedical and imaging applications, and advanced packaging. Our Wafer Services include the manufacture of silicon-based analog and mixed-signal ICs for our end markets. Our focus on the differentiated analog and complementary metal-oxide-semiconductor, or CMOS, markets supports long product life-cycles and requirements that value performance over cost-efficiencies, and leverages our portfolio IP.

Before we began independent operations, our fab was owned and operated by Cypress Semiconductor Corporation (“Cypress”) as a captive manufacturing facility. We have leveraged the Cypress system, manufacturing technology and process development capabilities to advance our product offerings. We became an independent company in March 2017 when we were acquired by Oxbow Industries, LLC, or Oxbow, as part of a divestiture from Cypress. Our multi-year Foundry Service Agreement with Cypress, which ended in June 2020, created a runway for us to operate the foundry at a high utilization rate while continuing to expand and diversify the customer base transferred by Cypress. Cypress was acquired in April 2020 by Infineon Technologies AG (“Infineon”).

Factors and Trends Affecting our Business and Results of Operations

The following trends and uncertainties either affected our financial performance during the first six months of 2022 and 2021 or are reasonably likely to impact our results in the future.

- Macroeconomic and competitive conditions, including cyclicalities and consolidation, affecting the semiconductor industry.
- The global economic climate, including the impact on the economy from geopolitical issues and the ongoing COVID-19 pandemic. Our business has been adversely affected by the effects of the COVID-19 pandemic. We implemented modifications to employee travel and employee work locations, as required, in some cases by federal, state and local authorities, which has had a negative impact on our employee productivity. As a result of the COVID-19 pandemic, one customer reduced its research and development expenditures with us, and a second customer experienced facility shutdowns which resulted in delays in project milestones, in each case negatively affecting our revenues. Because we have a manufacturing facility, we may be vulnerable to an outbreak of a new coronavirus or other contagious diseases. The effects of such an outbreak could include the temporary shutdown of our facilities, disruptions or restrictions on the ability to ship our products to our customers, as well as disruptions that may affect our suppliers. Any disruption of our ability to manufacture or distribute our products or of the ability of our suppliers to deliver key components on a timely basis could have material adverse effect on our revenue and operating results. See “Risk Factors—The effects of the COVID-19 outbreak could adversely affect our business, results of operations, and financial condition” in our Annual Report on Form 10-K and our condensed consolidated financial statements in this Quarterly Report on Form 10-Q for further information regarding the effects of the COVID-19 pandemic on our business.
- The impact of vaccine mandates on our workforce. In the U.S., the Food and Drug Administration issued emergency use authorization for COVID-19 vaccines and the government began extensive efforts to administer them. We have taken various steps to encourage and facilitate vaccination access for our employees, in accordance with federal guidance. We have provided flexibility for employees to get vaccinated, and strongly encouraged our workforce to take care of themselves and their colleagues. In September 2021, the White House issued an executive order and guidance from the Safer Federal Workforce Task Force broadly requiring many U.S.-based federal contractors to be fully vaccinated by December 8, 2021 (or to have an approved accommodation). In early November 2021, the federal government extended that deadline to January 18, 2022. On December 7, 2021, a federal district judge issued an order, temporarily suspending the government from enforcing the federal contractor mandate. That order is on appeal. State and local governments are also taking actions related to the pandemic, imposing additional and varying requirements on industry. We have taken, and are continuing to take, steps to encourage our employees to be fully vaccinated (or to have an approved accommodation) to protect our workplace and to position us to comply with the executive order, guidance, and related contract terms, if and as necessary, as we continue to evaluate the evolving situation and our customers’ requirements. Evolving government requirements, including regarding a vaccine mandate, along with the broader impacts of the continuing pandemic, could significantly impact our workforce and performance, as well as those of our suppliers, and result in costs that we may not be able to recover fully. We continue to take robust actions to protect the health, safety and well-being of our employees, and to serve our customers with continued

performance. See “Risk Factors—Vaccination or testing mandates could have a material adverse impact on our business and results of operations” in our Annual Report on Form 10-K for discussion of risks associated with the potential adverse effects on our business.

- On August 9, 2022, President Biden signed into law the Creating Helpful Incentives to Produce Semiconductors, or CHIPS, for America Act, in which the United States has committed to a renewed focus on providing incentives and funding for onshore companies to develop and advance the latest semiconductor technologies, supporting onshore manufacturing capabilities, and on strengthening key onshore supply chains. The act authorizes the Department of Commerce to enable execution of CHIPS awards and provides \$52.7 billion for American semiconductor research, development, manufacturing, and workforce development, including \$39 billion in financial assistance to build, expand, or modernize domestic facilities and equipment for semiconductor fabrication, assembly, testing, advanced packaging, or research and development.
- Our overall level of indebtedness from our revolving credit agreement for up to \$65 million, which we refer to as the Revolver, and a \$37 million financing from the sale of the land and building representing our headquarters in Minnesota, which we refer to as the Financing, the corresponding interest rates charged to us by our lenders and our ability to access borrowings under the Revolver.
- Identification and pursuit of specific product and geographic market opportunities that we find attractive both within and outside the United States. We will continue to more effectively address these opportunities through research and development and allocation of additional revenue and marketing resources.
- Material and other cost inflation. We strive for productivity improvements, and we implement increases in selling prices to help mitigate inflation. We expect the current economic environment will result in continuing price volatility and inflation for many of our raw materials. In addition, the labor market for skilled manufacturing remains tight and our labor costs have increased as a result.
- Supply chain disruptions impacting our business. We have experienced, and may continue to experience, supply chain disruption for substrates, chemicals and spare parts in addition to customer supply chain constraints that have negatively impacted our revenue.

Financial Performance Metrics

Our senior management team regularly reviews certain key financial performance metrics within our business, including:

- revenue and gross profit; and
- earnings before interest, taxes, depreciation and amortization, as adjusted, or adjusted EBITDA, which is a financial measure not prepared in accordance with accounting principles generally accepted in the United States, or U.S. GAAP, that excludes certain items that may not be indicative of our core operating results, as well as items that can vary widely across different industries or among companies within the same industry. For information regarding our non-GAAP financial measure, see the section entitled “—Non-GAAP Financial Measure” below.

Results of Operations

Second Quarter of 2022 Compared to the Second Quarter of 2021

The following table summarizes certain financial information relating to our operating results for the second quarter of 2022 and 2021.

	Second Quarter Ended			Percentage Change Favorable/ (Unfavorable)
	July 3, 2022 (1)	July 4, 2021 (1)	Dollar Change	
	(in thousands)			
Consolidated Statement of Operations Data:				
Revenue	\$ 47,407	\$ 41,189	\$ 6,218	15 %
Cost of revenue	45,327	39,377	5,950	(15)%
Gross profit	2,080	1,812	268	15 %
Research and development	2,361	3,339	(978)	29 %
Selling, general and administrative expenses	10,795	15,415	(4,620)	30 %
Change in fair value of contingent consideration	—	(942)	942	100 %
Operating income (loss)	(11,076)	(16,000)	4,924	31 %
Other income (expense):				
Paycheck Protection Program loan forgiveness	—	6,453	(6,453)	(100)%
Interest expense	(1,040)	(912)	(128)	(14)%
Total other income (expense)	(1,040)	5,541	(6,581)	(119)%
Loss before income taxes	(12,116)	(10,459)	(1,657)	(16)%
Income tax expense (benefit)	63	(4,237)	4,300	(101)%
Net loss	(12,179)	(6,222)	(5,957)	(96)%
Less: net income attributable to non-controlling interests	826	757	69	9 %
Net loss attributable to SkyWater Technology, Inc.	<u>\$ (13,005)</u>	<u>\$ (6,979)</u>	<u>\$ (6,026)</u>	<u>(86)%</u>
Other Financial Data:				
Adjusted EBITDA (2)	<u>\$ (1,602)</u>	<u>\$ (804)</u>	<u>\$ (798)</u>	<u>(99)%</u>

- (1) The consolidated statements of operations are for the second quarter of 2022 and the second quarter of 2021. The second quarter of 2022 and 2021 each contained 13 weeks.
- (2) See “—Non-GAAP Financial Measure” for the definition of adjusted EBITDA and reconciliation to the most directly comparable GAAP measure.

Six Months Ended July 3, 2022 Compared to the Six Months Ended July 4, 2021

The following table summarizes certain financial information relating to our operating results for the six months ended July 3, 2022 and for the six months ended July 4 2021.

	Six Months Ended		Dollar Change	Percentage Change Favorable/ (Unfavorable)
	July 3, 2022 (1)	July 4, 2021 (1)		
(in thousands)				
Consolidated Statement of Operations Data:				
Revenue	\$ 95,528	\$ 89,290	\$ 6,238	7 %
Cost of revenue	94,388	78,312	16,076	(21)%
Gross profit	1,140	10,978	(9,838)	(90)%
Research and development	4,643	5,266	(623)	12 %
Selling, general and administrative expenses	22,485	24,018	(1,533)	6 %
Change in fair value of contingent consideration	—	(886)	886	100 %
Operating loss	(25,988)	(17,420)	(8,568)	(49)%
Other income (expense):				
Paycheck Protection Program loan forgiveness	—	6,453	(6,453)	(100)%
Interest expense	(2,069)	(1,970)	(99)	(5)%
Total other income (expense)	(2,069)	4,483	(6,552)	(146)%
Loss before income taxes	(28,057)	(12,937)	(15,120)	(117)%
Income tax expense (benefit)	(131)	(4,662)	4,531	(97)%
Net loss	(27,926)	(8,275)	(19,651)	(237)%
Less: net income attributable to non-controlling interests	1,685	1,515	170	11 %
Net loss attributable to SkyWater Technology, Inc.	<u>\$ (29,611)</u>	<u>\$ (9,790)</u>	<u>\$ (19,821)</u>	<u>(202)%</u>
Other Financial Data:				
Adjusted EBITDA (2)	\$ (6,437)	\$ 4,825	\$ (11,262)	(233)%

- (1) The consolidated statements of operations are for the first six months of 2022 and the first six months of 2021. The first six months of 2022 and 2021 each contained 26 weeks.
- (2) See “—Non-GAAP Financial Measure” for the definition of adjusted EBITDA and reconciliation to the most directly comparable GAAP measure.

Revenue

Revenue was \$47.4 million for the second quarter of 2022 compared to \$41.2 million for the second quarter of 2021. The \$6.2 million or 15% increase was primarily driven by the growth in Advanced Technology Services programs and improved pricing terms for Wafer Services. Revenue was \$95.5 million for the first six months of 2022 and \$89.3 million for the first six months of 2021. The \$6.2 million or 7% increase was primarily the result of a new contract with a significant wafer services customer signed in the first quarter of 2022. As a result, we recorded revenue of \$8.2 million in the first quarter of 2022 to account for recognition of wafer services activities in process at the date the contract was signed.

The following table shows revenue by services type for the second quarters of 2022 and 2021 and the first six months of 2022 and 2021:

	Second Quarter Ended		Six Months Ended	
	July 3, 2022	July 4, 2021	July 3, 2022	July 4, 2021
(in thousands)				
Wafer Services	\$ 17,584	\$ 14,312	\$ 39,130	\$ 24,331
Advanced Technology Services	29,823	26,877	56,398	64,959
Total	<u>\$ 47,407</u>	<u>\$ 41,189</u>	<u>\$ 95,528</u>	<u>\$ 89,290</u>

The increase in Wafer Services revenue of \$3.3 million or 23% for the second quarter of 2022 was driven primarily by more favorable pricing and contract terms finalized with our largest customer at the end of the first quarter of 2022. For the six months ended July 3, 2022, Wafer Services revenue increased \$14.8 million, or 61%, primarily as a result of more favorable pricing and contract terms finalized with our largest customer at the end of first quarter of 2022, contributing \$8.2 million in revenue and more favorable pricing overall for our Wafer Services programs in 2022.

The increase in Advanced Technology Services revenues of \$2.9 million or 11% from the second quarter of 2021 to the second quarter of 2022 was primarily due to the overall growth in our Advanced Technology Services programs. For the six months ended July 3, 2022, Advanced Technology Services revenues decreased by \$8.6 million or 13%, primarily as a result of a decrease in the amount of revenue recognized related to services to qualify customer funded tool technologies. Tool revenue was \$1.3 million during the six months ended July 3, 2022 compared to \$17.8 million during the six months ended July 4, 2021. The decrease was partially offset by the overall growth in our Advanced Technology Services programs in 2022.

Gross profit

Gross profit increased \$0.3 million, or 15%, to \$2.1 million for the second quarter of 2022, from \$1.8 million for the second quarter of 2021. The increase was primarily due to a more favorable revenue mix, partially offset by an increase in inflationary costs related to both materials and labor. For the six months ended July 3, 2022, gross profit declined to \$1.1 million from \$11.0 million for the six months ended July 4, 2021. The decrease of \$9.9 million was primarily attributable to the decrease in gross profit on tool revenues, which declined by \$6.5 million or 98% from the six months ended July 4, 2021. In addition, gross profit declined as a result of an increase in inflationary costs in 2022 related to both materials and labor.

Research and development

Research and development costs decreased to \$2.4 million for the second quarter of 2022, from \$3.4 million for the second quarter of 2021. The decrease of \$1.0 million, or 29%, was primarily attributable to a decrease in equity-based compensation expense of \$1.4 million, partially offset by an increase of \$0.5 million in personnel expense, due to our continued investment in internal personnel and external engineering support. For the six months ended July 3, 2022, research and development costs decreased to \$4.6 million from \$5.3 million for the six months ended July 4, 2021. The decrease of \$0.7 million was primarily attributable to a decrease in equity-based compensation of \$1.1 million, partially offset by \$0.3 million increase in personnel expense as a result of our continued investment in internal personnel.

Selling, general and administrative expenses

Selling, general and administrative expenses decreased to \$10.8 million for the second quarter of 2022, from \$15.4 million for the second quarter of 2021. The decrease of \$4.6 million, or 30%, was primarily attributable to a decrease of \$3.0 million in equity-based compensation expense and a decrease of \$1.8 million in labor expense as a result of the bonus program which took place in the second quarter of 2021 related to the IPO completed during that quarter. These decreases were partially offset by an increase of \$0.2 million in personnel expense as a result of our continued investment in internal personnel. For the six months ended July 3, 2022, selling, general and administrative expenses decreased to \$22.5 million from \$24.0 million for the six months ended July 4, 2021. The decrease of \$1.5 million was primarily attributable to a decrease in equity-based compensation of \$1.3 million.

Income tax expense (benefit)

Income taxes increased to \$0.1 million expense for the second quarter of 2022, from a benefit of \$4.2 million for the second quarter of 2021. The effective income tax rate for the second quarter of 2022 was (0.5)%, compared to an effective income tax rate of 40.5% for the second quarter of 2021.

Income taxes benefit decreased to \$0.1 million benefit for the six months ended July 3, 2022 from a \$4.7 million benefit for the six months ended July 4, 2021. The effective income tax rate for the six months ended July 3, 2022 was 0.5%, compared to an effective income tax rate of 36.0% for the six months ended July 4, 2021. The effective income tax rate applied to our pre-tax loss was lower for the second quarter of 2022 than our statutory tax rate of 21% primarily due to deferred tax asset valuation allowances. The income tax rate applied to our pre-tax loss was higher for the three and six months ended July 4, 2021 than our statutory tax rate of 21% primarily due to the gain realized as a result of the proceeds received from the paycheck protection loan forgiveness program.

Net income attributable to non-controlling interests

Net income attributable to non-controlling interests remained flat for the second quarter of 2022 and 2021 and increased slightly by \$0.2 million from the six months ended July 4, 2021 to the six months ended July 3, 2022. Net income attributable to non-controlling interests reflects the net income of the variable interest entity, or VIE, that we consolidate, representing the

economic interest in the profits and losses of Oxbow Realty that the owners of our shareholders' equity do not legally have rights or obligations to.

Adjusted EBITDA

Adjusted EBITDA decreased \$0.8 million, or 99%, to \$(1.6) million for the second quarter of 2022 from \$(0.8) million for the second quarter of 2021. For the six months ended July 3, 2022, Adjusted EBITDA decreased \$11.2 million to \$(6.4) million from \$4.8 million for the six months ended July 4, 2021. The decrease in adjusted EBITDA for both the second quarter of 2022 and the six months ended July 3, 2022 primarily reflects decreased gross profit due to increased labor and infrastructure costs as we continue to scale our business to meet the demands of our customers and the requirements of being a public company. For a discussion of adjusted EBITDA as well as a reconciliation to the most directly comparable U.S. GAAP measure, see the section below entitled “—Non-GAAP Financial Measure.”

Liquidity and Capital Resources

General

Our ability to execute our operating strategy is dependent on our ability to maintain liquidity and continue to access capital through our Revolver (as defined in Note 6 – *Debt* to the Condensed Consolidated Financial Statements) and other sources of financing. Our current business plans indicate that we will require additional liquidity to continue our operations for the next 12 months from the issuance of the consolidated financial statements. In response to this, we plan to pursue additional debt and equity financing, and are implementing a plan to reduce operating costs to improve cash flow, which includes a reduction in spending and a delayed increase in personnel, and may require us to decrease our level of investment in new products and technologies, discontinue further expansion of our business, or scale back our existing operations. Additionally, the Company obtained a support letter from Oxbow, an affiliate of our principal stockholder, to provide funding in an amount up to \$12.5 million, if necessary, to enable the Company to meet its obligations as they become due through at least one year and a day beyond the issuance of these financial statements on August 17, 2022. Management believes that based upon its operational forecasts, cash and cash equivalents on hand, available borrowings on our Revolver, cost reduction measures and the support letter from an affiliate of our principal stockholder, as needed, will provide sufficient liquidity to fund its operations for the next 12 months from the issuance of the consolidated financial statements.

The Company has based this estimate on assumptions that may prove to be wrong, and its operating plan may change as a result of many factors currently unknown to it. To the extent that our current resources and plans to reduce expenses are insufficient to satisfy our cash requirements, we may need to seek additional equity or debt financing. Our ability to do so depends on prevailing economic conditions and other factors, many of which are beyond our control.

We had \$10.7 million in cash and cash equivalents, not including cash held by a variable interest entity that we consolidate, and availability under our Revolver of \$17.6 million as of July 3, 2022. However, we must maintain availability under the Revolver of at least \$15 million in order to not have to comply with the leverage ratio and fixed charge coverage ratio financial covenants contained in the Revolver with respect to the fiscal quarters ending on or prior to July 3, 2023.

Initial Public Offering

On April 23, 2021, we completed our IPO and issued 8,004,000 shares of common stock, including the underwriter's exercise of their right to purchase additional shares, at an initial offering price to the public of \$14.00 per share. We received net proceeds from the IPO of approximately \$100.2 million, after deducting underwriting discounts and commissions and offering costs of approximately \$11.9 million. We estimate that we utilized approximately \$45 million of our IPO proceeds to pay down our revolving credit agreement, approximately \$28 million of our IPO proceeds to fund capital expenditures, and approximately \$27 million of our IPO proceeds to fund our operating activities.

Capital Expenditures

On July 26, 2021, we announced that our Board of Directors approved \$56 million in strategic capital investments for expanding manufacturing capacity and technology capabilities at our Minnesota facility. The majority of this investment is targeted to expand capacity and capabilities at our Minnesota fab which is expected to increase overall output by at least 40% and to enable accelerated revenue growth. The remainder is focused on expediting our entry into the gallium nitride, or GaN, market, a promising technology for electric vehicles, 5G and consumer electronics, among others due to its properties that enable higher charging efficiencies, smaller ship size, and lighter weight for many applications. We believe SkyWater can fill the need for a US-based 200 mm foundry to offer technology services for GaN-based solutions expanding the serviceable market for our technology-as-a-serviceSM model. The strategic capital investment is a multi-year strategy and we invested approximately \$15.8 million during 2021 and the first six months of 2022.

For the first six months of 2022, we spent approximately \$5.9 million on capital expenditures, including purchases of property, equipment and software. The majority of these capital expenditures relate to our foundry expansion in Minnesota, as discussed below, and the development of our advanced packaging capabilities at the Center for NeoVation in Florida. We anticipate our cash on hand and the availability under our Revolver will provide the funds needed to meet our customer demand and anticipated capital expenditures in 2022.

We have approximately \$12 million of contractual commitments relating to various anticipated capital expenditures outstanding as of July 3, 2022 that we expect to be paid in the remainder of 2022, through either cash on hand or availability under our Revolver. On April 1, 2022, we commenced a finance lease for a nitrogen generator. The lease has a term of 15 years for total fixed payments of approximately \$14 million.

Contingent Consideration

We paid \$0.4 on the remaining obligation related to our contingent consideration royalty liability in the first half of 2022. We anticipate our cash on hand and availability under our Revolver will provide the funds necessary to settle the contingent consideration royalty liability.

Working Capital

Historically, we have depended on cash on hand, funds available under our Revolver and in the future may depend on additional debt and equity financings, similar to our IPO, to finance our expansion strategy, working capital needs and capital expenditures. We believe that these sources of funds will be adequate to provide cash, as required, to support our strategy, ongoing operations, capital expenditures, lease obligations and working capital for at least the next 12 months. However, we cannot be certain that we will be able to obtain future debt or equity financings adequate for our cash requirements on commercially reasonable terms or at all.

As of July 3, 2022, we had available aggregate undrawn borrowing capacity of approximately \$18 million under our Revolver. However, we must maintain availability under the Revolver of at least \$15 million in order to not have to comply with the leverage ratio and fixed charge coverage ratio financial covenants contained in the Revolver with respect to the fiscal quarters ending on or prior to July 2, 2023. For the periods presented, our use of cash was primarily driven by our investing activities, and specifically by our investments in capital expenditures.

The following table sets forth general information derived from our condensed consolidated statement of cash flows for the first six months of 2022 and 2021:

	Six Months Ended	
	July 3, 2022	July 4, 2021
	(in thousands)	
Net cash used in operating activities	\$ (13,862)	\$ (30,811)
Net cash used in investing activities	\$ (5,863)	\$ (13,255)
Net cash provided by financing activities	\$ 17,782	\$ 101,233

Cash and Cash Equivalents

At July 3, 2022 and January 2, 2022, we had \$11.0 million and \$12.9 million of cash and cash equivalents, respectively, including cash of \$0.3 million and \$0.5 million, respectively, held by a variable interest entity that we consolidate.

Operating Activities

Cash flow from operations is driven by changes in the working capital needs associated with the various goods and services we provide, and expenses related to the infrastructure in place to support revenue generation. Working capital is primarily affected by changes in accounts receivable, accounts payable, accrued expenses, and deferred revenue, all of which tend to be related and are affected by changes in the timing and volume of work performed and our increased expenditures as a public company. Net cash used in operating activities was \$13.9 million during the first six months of 2022, a decrease of \$16.9 million from \$30.8 million of cash used in operating activities during the first six months of 2021. The decrease in cash provided by operating activities during the first six months of 2022 was driven primarily by an increase in our costs as described in *Gross profit* above. Our operating cash flow was additionally impacted from the change in our working capital accounts. Deferred revenue decreased during the first six months of 2022 as we recognized revenue from customers who funded our building expansion during 2020.

Investing Activities

Capital expenditures are a significant use of our capital resources. These investments are intended to enable revenue growth in new and expanding markets, help us meet product demand and increase our manufacturing efficiencies and capacity.

Net cash used in investing activities was \$5.9 million during the first six months of 2022, a decrease of \$7.4 million from \$13.3 million during the first six months of 2021. The decrease in cash used during the first six months of 2022 reflects decreased capital spending on property and equipment as we fully complete our foundry expansion project to increase manufacturing capacity at our Minnesota facility.

Financing Activities

Net cash provided by financing activities was \$17.8 million during the first six months of 2022, a decrease of \$83.4 million from net cash provided by financing activities of \$101.2 million during the first six months of 2021. The decrease in net cash provided by financing activities during the first six months of 2022 was primarily driven by the proceeds received from the issuance of common stock pursuant to the initial public offering which occurred in the second quarter of 2021. Partially offsetting this decrease was an increase in net proceeds on our revolver, which amounted to \$18.9 million during the first six months of 2022 compared to \$0.4 million during the first six months of 2021. The decrease was additionally driven by a decrease in distributions to our VIE and partially offset from proceeds from our employee stock purchase plan and our long term incentive plan.

Indebtedness

Sale Leaseback Transaction

On September 29, 2020, we entered into an agreement to sell the land and building representing our primary operating location in Bloomington, Minnesota to Oxbow Realty, LLC, or Oxbow Realty, an entity controlled by our principal stockholder for \$39 million, less applicable transaction costs of \$1.5 million and transaction services fees paid to Oxbow Realty of \$2.0 million and paid a guarantee fee to our principal stockholder of \$2.0 million. We subsequently entered into an agreement to lease the land and building from Oxbow Realty for initial payments of \$0.4 million per month over 20 years. The monthly payments are subject to a 2% increase each year during the term of the lease. We are also required to make certain customary payments constituting "additional rent," including certain monthly reserve, insurance and tax payments, in accordance with the terms of the lease. Due to our continuing involvement in the property, we are accounting for the transactions as a failed sale leaseback (a financing transaction). Under failed sale leaseback accounting, we are deemed the owner of the property with the proceeds received recorded as a financial obligation.

Revolving Credit Agreement

On December 28, 2020, we entered into an amended and restated revolving credit agreement with Wells Fargo, our Revolver, of up to \$65 million that replaced our previous line of credit and term loan. Under the agreement, the facility is available on a revolving basis, subject to availability under a borrowing base consisting of a percentage of eligible accounts receivable, inventory and owned equipment. The Revolver is secured by a security interest in substantially all of our accounts receivable, inventory and equipment. The Revolver can be repaid and borrowed again at any time without penalty or premium until the maturity date of December 28, 2025. The Revolver is available for issuance of letters of credit to a specified limit of \$10 million.

Under the Revolver, we can elect the base rate (greatest of the federal funds rate plus 0.5%, LIBOR for a one-month period plus 1%, or the institution's prime rate) or LIBOR for a period of one, two, three or six months as selected by us, plus a margin depending on the amount of borrowings outstanding. We will also pay a commitment fee equal to 0.25% to 0.375% of the average commitment not utilized, depending on the amount not utilized. Interest payments are due monthly.

On November 3, 2021, we entered into an amendment to the Revolver, effective as of October 1, 2021, to eliminate the requirement for us to comply with the leverage ratio financial covenant contained therein with respect to the fiscal quarters ending on or prior to July 2, 2023, so long as the remaining availability under the Revolver has equaled or exceeded \$15 million. Certain financial covenants, including a fixed charge coverage ratio and leverage ratio, become applicable only if unused remaining availability falls below \$15 million. As of July 3, 2022, our unused remaining availability was \$18 million and we were in compliance with applicable financial covenants of the Revolver and expect to be in compliance with applicable financial covenants over the next twelve months. The fixed charge coverage ratio financial covenant requires us to maintain a fixed charge coverage ratio of at least 1.1 to 1.0 on a rolling twelve-month basis. The fixed charge coverage ratio included in our credit agreement is defined as (A) earnings before interest, taxes, depreciation and amortization ("EBITDA"), less unfinanced capital expenditures, divided by (B) fixed charges, which are generally defined as cash interest and income taxes, scheduled principal payments on loans and contingent consideration arrangements, and restricted payments such as dividends.

EBITDA, as defined, includes adjustments for such items as unusual gains or losses, equity-based compensation and management fees, as well as other adjustments. The leverage ratio financial covenant requires us to maintain a leverage ratio of no greater than 3.0 to 1.0 on a rolling twelve-month basis measured quarterly. The leverage ratio included in our credit agreement is defined as our funded indebtedness as of the measurement date divided by our EBITDA for the twelve-month period as of the measurement date.

The Revolver contains covenants, including restrictions on indebtedness, liens, mergers, consolidations, investments, acquisitions, disposition of assets, and transactions with affiliates. Dividends, redemptions and other payments on equity (restricted payments) are limited to (1) restricted payments to the loan parties, and (2) declaring and making dividend payments or other distributions payable solely in capital stock. Customary events of default (with customary grace periods, notice and cure periods and thresholds) include payment default, breach of representation in any material respect, breach of certain covenants, default to material indebtedness, bankruptcy, ERISA violations, material judgments, change in control and termination or invalidity of guaranty or security documents.

Contractual Obligations

There were no significant changes outside the ordinary course of business in our contractual obligations from those disclosed in Item 7, “Management’s Discussion and Analysis of Financial Condition and Results of Operations - Material Cash Requirements” of our Annual Report on Form 10-K for the fiscal year ended January 2, 2022.

JOBS Act

We qualify as an “emerging growth company” pursuant to the provisions of the JOBS Act. For as long as we are an “emerging growth company,” we may take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not “emerging growth companies,” including, but not limited to, not being required to comply with the auditor attestation requirements of Section 404 of the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements, exemptions from the requirements of holding advisory “say-on-pay” votes on executive compensation and shareholder advisory votes on golden parachute compensation.

The JOBS Act also permits an emerging growth company like us to take advantage of an extended transition period to comply with new or revised accounting standards applicable to public companies. We have elected to use the extended transition period for complying with new or revised accounting standards and, therefore, we will not be subject to the same new or revised accounting standards as other public companies that comply with such new or revised accounting standards on a non-delayed basis.

Critical Accounting Policies and Estimates

In connection with preparing our condensed consolidated financial statements in accordance with U.S. GAAP, we are required to make assumptions and estimates about future events and apply judgments that affect the reported amounts of assets, liabilities, revenue and expense, and the related disclosures. We base our assumptions, estimates and judgments on historical experience, current trends and other factors that management believes to be relevant at the time we prepare our condensed consolidated financial statements. On a regular basis, management reviews the accounting policies, assumptions, estimates and judgments to ensure that our condensed consolidated financial statements are presented fairly and in accordance with U.S. GAAP. However, because future events and their effects cannot be determined with certainty, actual results could differ materially from our assumptions and estimates.

On an ongoing basis, management evaluates its estimates, including those related to revenue recognition, valuation of long-lived assets and inventory, share-based compensation and income taxes. We base our estimates and judgments on historical experience and on various other factors that we believe to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may materially differ from these estimates under different assumptions or conditions.

There have been no material changes to our critical accounting policies and estimates disclosed in our Annual Report on Form 10-K for the year ended January 2, 2022, except as set forth below.

Revenue Recognition of New Wafer Services Contract

Revenue is recognized either over time as work progresses using an output measure or at a point-in-time, depending upon contract-specific terms and the pattern of transfer of control of the product or service to the customer. Due to the nature of our contracts, there can be judgment involved in determining the performance obligations that are included in the related contract. We analyze each contract to conclude what enforceable rights and obligations exist between us and our customers. In

doing so, we determine our unit of account by identifying the promises within the contract that are both (1) considered to be distinct and (2) distinct within the context of each contract.

In March 2022, we signed a new contract with a significant wafer services customer. Under the contract, orders are non-cancellable and we have an enforceable right to complete the orders and to payment for any finished or in-process wafers plus a reasonable margin. The wafers produced for that customer are highly customized and have no alternative use to us. Control of these wafers is deemed to transfer to the customer over time during the fabrication process, using the same measure of progress toward satisfying the promise to deliver the units to the customer. Consequently, the transaction price is recognized as revenue over time based on actual costs incurred in the fabrication process to date relative to total expected costs to produce all wafers beginning in March 2022. The contract terms and pricing is applicable to all in-process and future wafer. We recorded revenue of \$8,230 in the first six months of 2022 to account for recognition of wafer services activities in process at the date the contract was signed. Additionally, this change in the timing of revenue recognition reduced our work-in-process inventory and increased our unbilled receivables (contract assets) and cost of revenue. Under the previous contract with the significant customer, we were recognizing revenue at a point-in-time under a bill and hold arrangement as disclosed in our Annual Report on Form 10-K for the year ended January 2, 2022.

Recent Accounting Pronouncements

For a description of our recently adopted accounting pronouncements and recently issued accounting standards not yet adopted, see “Note 3 — *Summary of Significant Accounting Policies*” to the condensed consolidated financial statements included in Part I, Item 1 of this Quarterly Report on Form 10-Q.

Non-GAAP Financial Measure

Our condensed consolidated financial statements are prepared in accordance with U.S. GAAP. To supplement our condensed consolidated financials presented in accordance with U.S. GAAP, an additional non-GAAP financial measure is provided and reconciled in the following table.

We provide supplemental non-GAAP financial information that our management utilizes to evaluate our ongoing financial performance and provide additional insight to investors as supplemental information to our U.S. GAAP results. We use adjusted EBITDA to provide a baseline for analyzing trends in our business and to exclude certain items that may not be indicative of our core operating results. The use of non-GAAP financial information should not be considered as an alternative to, or more meaningful than, the comparable U.S. GAAP measure. In addition, because our non-GAAP measure is not determined in accordance with U.S. GAAP, it is susceptible to differing calculations, and not all comparable or peer companies may calculate their non-GAAP measures in the same manner. As a result, the non-GAAP financial measure presented in this Quarterly Report on Form 10-Q may not be directly comparable to similarly titled measures presented by other companies.

This non-GAAP financial measure should not be considered as an alternative to, or more meaningful than, net income determined in accordance with U.S. GAAP.

Adjusted EBITDA

Adjusted EBITDA is not a financial measure determined in accordance with U.S. GAAP. We define adjusted EBITDA as net income before interest expense, income tax provision (benefit), depreciation and amortization, equity-based compensation and certain other items that we do not view as indicative of our ongoing performance, including fair value changes in contingent consideration, management fees, inventory write-down, corporate conversion and IPO related costs, Paycheck Protection Program Loan forgiveness, SkyWater Florida start-up costs, net income attributable to non-controlling interests, and management transition expense.

We believe adjusted EBITDA is a useful performance measure because it allows for an effective evaluation of our operating performance when compared to our peers, without regard to our financing methods or capital structure. We exclude the items listed above from net income in arriving at adjusted EBITDA because these amounts can vary substantially within our industry depending upon accounting methods and book values of assets, capital structures and the method by which the assets were acquired. Adjusted EBITDA should not be considered as an alternative to, or more meaningful than, net income determined in accordance with U.S. GAAP. Certain items excluded from adjusted EBITDA are significant components in understanding and assessing a company’s financial performance, such as a company’s cost of capital and tax structure, as well as the historic costs of depreciable assets, none of which are reflected in adjusted EBITDA. Our presentation of adjusted EBITDA should not be construed as an indication that our results will be unaffected by the items excluded from adjusted EBITDA. In future fiscal periods, we may exclude such items and may incur income and expenses similar to these excluded items. Accordingly, the exclusion of these items and other similar items in our non-GAAP presentation should not be interpreted as implying that these items are non-recurring, infrequent or unusual, unless otherwise expressly indicated.

The following table presents a reconciliation of net income (loss) to adjusted EBITDA, our most directly comparable financial measure calculated and presented in accordance with U.S. GAAP.

	Second Quarter Ended		Six Months Ended	
	July 3, 2022	July 4, 2021	July 3, 2022	July 4, 2021
	(in thousands)			
Net loss attributable to SkyWater Technology, Inc.	\$ (13,005)	\$ (6,979)	\$ (29,611)	\$ (9,790)
Interest expense	1,040	912	2,069	1,970
Income tax (benefit) expense	63	(4,237)	(131)	(4,662)
Depreciation and amortization	7,198	6,854	13,657	13,336
EBITDA	(4,704)	(3,450)	(14,016)	854
Paycheck Protection Program loan forgiveness	—	(6,453)	—	(6,453)
Corporate conversion and initial public offering related costs	—	1,521	—	1,521
SkyWater Florida start-up costs ⁽¹⁾	158	504	560	504
Management transition expense	—	435	—	435
Fair value changes in contingent consideration ⁽²⁾	—	(942)	—	(886)
Equity-based compensation ⁽³⁾	2,118	6,768	5,334	7,003
Management fees ⁽⁴⁾	—	56	—	332
Net income attributable to non-controlling interests ⁽⁵⁾	826	757	1,685	1,515
Adjusted EBITDA	<u>\$ (1,602)</u>	<u>\$ (804)</u>	<u>\$ (6,437)</u>	<u>\$ 4,825</u>

- (1) Represents start-up costs associated with our 200 mm advanced packaging facility in Kissimmee, Florida, which includes legal fees, recruiting expenses, retention awards and facility start-up expenses. These expenses are not indicative of our ongoing costs and will be discontinued following completion of the start-up of SkyWater Florida.
- (2) Represents non-cash valuation adjustment of contingent consideration to fair market value during the period.
- (3) Represents non-cash equity-based compensation expense.
- (4) Represents a related party transaction with Oxbow, our principal stockholder. As these fees are not part of the core business, did not continue after our IPO and are excluded from management's assessment of the business, we believe it is useful to investors to view our results excluding these fees.
- (5) Represents net income attributable to our VIE, which was formed for the purpose of purchasing our land and building with the proceeds of a bank loan. Since depreciation and interest expense are excluded from net loss in our adjusted EBITDA financial measure, we also exclude the net income attributable to the VIE.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Market risk is the risk of loss arising from adverse changes in market rates and prices. Currently, our market risks relate to potential changes in the fair value of our debt due to fluctuations in applicable market interest rates. In the future, our market risk exposure generally will be limited to those risks that arise in the normal course of business, as we do not engage in speculative, non-operating transactions, nor do we utilize financial instruments or derivative instruments for trading purposes.

Credit Risk

Financial instruments that potentially subject us to credit risk are cash and cash equivalents and accounts receivable. Cash balances are maintained in financial institutions, which at times exceed federally insured limits. We monitor the financial condition of the financial institutions in which our accounts are maintained and have not experienced any losses in such accounts. We perform ongoing credit evaluations as to the financial condition of our customers with respect to trade receivables. Generally, no collateral is required as a condition of sale. Our consideration of the need for an allowance for doubtful accounts is based upon current market conditions and other factors.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our President and Chief Executive Officer and our Chief Financial Officer, our principal executive officer and principal financial officer, respectively, have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of July 3, 2022.

Disclosure controls and procedures are controls and other procedures that are designed to ensure that information required to be disclosed in our reports filed or submitted under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. Disclosure controls and procedures include controls and procedures designed to ensure that information required to be disclosed in our reports filed under the Exchange Act is accumulated and communicated to management, including our President and Chief Executive Officer and our Chief Financial Officer, to allow timely decisions regarding required disclosure. Based on the evaluation of our disclosure controls and procedures, our President and Chief Executive Officer and our Chief Financial Officer concluded that our disclosure controls and procedures were not effective as of July 3, 2022 due to the material weaknesses in our internal control over financial reporting described below. In light of this fact, our management has performed additional analyses, reconciliations, and other post-closing procedures and has concluded that, notwithstanding the material weaknesses in our internal control over financial reporting, the condensed consolidated financial statements for the periods covered by and included in this Quarterly Report on Form 10-Q fairly present, in all material respects, our financial position, results of operations and cash flows for the periods presented in conformity with U.S. GAAP.

Previously Reported Material Weaknesses in Internal Control over Financial Reporting

As disclosed in Item 9A. "Controls and Procedures" in our Annual Report on Form 10-K for the year ended January 2, 2022, we previously identified material weaknesses in our internal control over financial reporting. As of July 3, 2022, we have material weaknesses in components of the COSO framework, including the control environment and risk assessment due to our limited accounting and finance resources, which resulted in inappropriate preparation, review and maintenance of documentation and information that is critical to the design and consistent execution and monitoring of internal controls. We did not sufficiently design, implement, and maintain control activities related to the recording of revenue to sufficiently assess the obligations for proper accounting, review of the completion of performance obligations and recognition of revenue. These material weaknesses could result in a misstatement of account balances or disclosures that would result in a material misstatement to the annual or interim financial statements that would not be prevented or detected. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the annual or interim financial statements will not be prevented or detected on a timely basis.

Remediation Plan

To address our material weaknesses, we have developed a 2022 Sarbanes-Oxley 404 Remediation Plan which includes the various timing for implementation and documentation of policies, procedures, and controls across all our various processes. In executing the remediation plan, we have created additional roles within the financial reporting group. Certain of these roles have been filled with permanent employees and others with contractors while we search for permanent employees. The individuals who filled these roles have significant Sarbanes-Oxley experience. In addition, collectively, they have several years of experience in the public accounting sector as well as working with large public companies who are compliant with Sarbanes Oxley 404.

Also, in the second quarter of 2022, we have completed the design of the internal controls in the financial reporting and revenue accounting areas. While we believe that these efforts have improved our internal control over financial reporting and revenue, our remediated controls will require the testing of the operating effectiveness over a sustained period of time to conclude they are remediated.

The actions that we are taking are subject to ongoing senior management review, as well as audit committee oversight. We will not be able to conclude whether the steps we are taking will fully remediate the material weaknesses in our internal control over financial reporting until we have completed our remediation efforts and subsequent evaluation of their effectiveness. Until these weaknesses are remediated, we plan to continue to perform additional analyses and other procedures to ensure that our condensed consolidated financial statements are prepared in accordance with U.S. GAAP.

Changes in Internal Control Over Financial Reporting

Other than completion of the design of the internal controls in the financial reporting and revenue accounting areas and the creation of the additional roles within the financial reporting group, as discussed above, there was no change in our internal control over financial reporting that occurred during our most recently completed fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

We are not presently a party to any litigation the outcome of which, we believe, if determined adversely to us, would individually or taken together have a material adverse effect on our business, operating results, cash flows or financial condition.

Item 1A. Risk Factors

This Quarterly Report on Form 10-Q should be read in conjunction with the risk factors included in Item 1A. “Risk Factors” our Annual Report on Form 10-K for the year ended January 2, 2022. There have been no material changes to the risk factors disclosed under the heading “Risk Factors” in our Annual Report on Form 10-K for the year ended January 2, 2022.

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

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6. Exhibits

The following is a list of all exhibits filed or furnished as part of this report:

Exhibit Number	Description
3.1	Certificate of Incorporation of SkyWater Technology, Inc. (incorporated by reference to the Company’s Registration Statement on Form S-1 filed with the SEC on April 12, 2021)
3.2	Bylaws of SkyWater Technology, Inc. (incorporated by reference to the Company’s Registration Statement on Form S-1 filed with the SEC on April 12, 2021)
31.1	Certification of the Chief Executive Officer pursuant to Exchange Act Rules Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of the Chief Financial Officer pursuant to Exchange Act Rules Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1*	Certification of the Chief Executive Officer pursuant to 18 U.S.C. Section 1350
32.2*	Certification of the Chief Financial Officer pursuant to 18 U.S.C. Section 1350
101.INS	Inline XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document
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
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)

- * The certifications furnished in Exhibit 32.1 and Exhibit 32.2 hereto are deemed to accompany this Quarterly Report on Form 10-Q and will not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, except to the extent that the registrant specifically incorporates it by reference.

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.

SkyWater Technology, Inc.

Date: August 17, 2022

By: /s/ Thomas Sonderman

Thomas Sonderman
President and Chief Executive Officer
(Principal Executive Officer)

By: /s/ Steve Manko

Steve Manko
Chief Financial Officer
(Principal Financial Officer and Principal Accounting Officer)