

Wayfair Inc.
Form 10-Q
November 01, 2018
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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 September 30, 2018

OR

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

For the transition period from _____ to _____

Commission File Number: 001-36666

Wayfair Inc.

(Exact name of registrant as specified in its charter)

Delaware 36-4791999

(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification Number)

4 Copley Place, 7th Floor, Boston, MA 02116
(Address of principal executive offices) (Zip Code)
(617) 532-6100

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer 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 13(a) of the Exchange Act.

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Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Class

Outstanding at October 24, 2018

Class A Common Stock, \$0.001 par value per share 61,804,108

Class B Common Stock, \$0.001 par value per share 28,539,198

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For the Quarterly Period Ended September 30, 2018

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PART I

FINANCIAL INFORMATION

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

This Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the "Securities Act"), and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). All statements other than statements of historical fact contained in this Quarterly Report on Form 10-Q, including statements regarding our future results of operations and financial position, business strategy and plans and objectives of management for future operations, are forward-looking statements. In some cases, you can identify forward-looking statements by terms such as "may," "will," "should," "expects," "plans," "anticipates," "could," "intends," "target," "projects," "contemplates," "believes," "estimates," "predicts," "potential" or "continue" or the negative of these terms or other similar expressions.

Forward-looking statements are based on current expectations of future events. We cannot guarantee that any forward-looking statement will be accurate, although we believe that we have been reasonable in our expectations and assumptions. Investors should realize that if underlying assumptions prove inaccurate or that known or unknown risks or uncertainties materialize, actual results could vary materially from the Company's expectations and projections. Investors are therefore cautioned not to place undue reliance on any forward-looking statements. These forward-looking statements speak only as of the date of this Quarterly Report on Form 10-Q and, except as required by applicable law, we undertake no obligation to publicly update or revise any forward-looking statements contained herein, whether as a result of any new information, future events or otherwise.

Factors that could cause or contribute to differences in our future results include, without limitation, the following:

- our ability to acquire new customers and sustain and/or manage our growth;
- our ability to increase our net revenue per active customer;
- our ability to build and maintain strong brands;
- our ability to manage our global growth and expansion;
- our ability to compete successfully;
- the rate of growth of the Internet and e-commerce;
- economic factors, such as interest rates, currency exchange fluctuations and changes in customer spending;
- world events, natural disasters, public health emergencies, civil disturbances, and terrorist attacks; and
- developments in, and the outcome of, legal and regulatory proceedings and investigations to which we are a party or are subject, and the liabilities, obligations and expenses, if any, that we may incur in connection therewith.

A further list and description of risks, uncertainties and other factors that could cause or contribute to differences in our future results include the cautionary statements herein and in our other filings with the Securities and Exchange Commission, including those set forth under Part II, Item 1A, Risk Factors of this Quarterly Report on Form 10-Q and in our Annual Report on Form 10-K for the fiscal year ended December 31, 2017. We qualify all of our forward-looking statements by these cautionary statements.

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WAYFAIR INC.
CONSOLIDATED AND CONDENSED BALANCE SHEETS
(In thousands, except share and per share data)
(Unaudited)

| | September 30, 2018 | December 31, 2017 |
|---|--------------------------|-------------------------|
| Assets | | |
| Current assets | | |
| Cash and cash equivalents | \$488,636 | \$558,960 |
| Short-term investments | 30,056 | 61,032 |
| Accounts receivable, net of allowance of \$7,462 and \$7,000 at September 30, 2018 and December 31, 2017, respectively | 41,013 | 37,948 |
| Inventories | 35,723 | 28,042 |
| Prepaid expenses and other current assets | 167,754 | 130,838 |
| Total current assets | 763,182 | 816,820 |
| Property and equipment, net | 509,661 | 361,141 |
| Goodwill and intangible assets, net | 2,724 | 3,105 |
| Long-term investments | 6,521 | 21,561 |
| Other noncurrent assets | 17,550 | 10,776 |
| Total assets | \$1,299,638 | \$1,213,403 |
| Liabilities and Stockholders' Equity | | |
| Current liabilities | | |
| Accounts payable | \$591,931 | \$440,366 |
| Accrued expenses | 167,745 | 120,247 |
| Deferred revenue | 133,423 | 94,116 |
| Other current liabilities | 109,212 | 85,026 |
| Total current liabilities | 1,002,311 | 739,755 |
| Lease financing obligation, net of current portion | 184,055 | 82,580 |
| Long-term debt | 346,641 | 332,905 |
| Other liabilities | 78,852 | 106,492 |
| Total liabilities | 1,611,859 | 1,261,732 |
| Commitments and contingencies (Note 6) | | |
| Convertible preferred stock, \$0.001 par value per share: 10,000,000 shares authorized and none issued at September 30, 2018 and December 31, 2017 | — | — |
| Stockholders' equity: | | |
| Class A common stock, par value \$0.001 per share, 500,000,000 shares authorized, 61,400,416 and 57,398,983 shares issued and outstanding at September 30, 2018 and December 31, 2017, respectively | 61 | 57 |
| Class B common stock, par value \$0.001 per share, 164,000,000 shares authorized, 28,726,124 and 30,809,627 shares issued and outstanding at September 30, 2018 and December 31, 2017, respectively | 29 | 31 |
| Additional paid-in capital | 628,600 | 537,212 |
| Accumulated deficit | (938,844) | (583,266) |
| Accumulated other comprehensive (loss) | (2,067) | (2,363) |
| Total stockholders' equity | (312,221) | (48,329) |
| Total liabilities and stockholders' equity | \$1,299,638 | \$1,213,403 |

The accompanying notes are an integral part of these Unaudited Consolidated and Condensed Financial Statements.

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WAYFAIR INC.

CONSOLIDATED AND CONDENSED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

(Unaudited)

| | Three months ended | | Nine months ended | |
|--|--------------------|-------------|-------------------|--------------|
| | September 30, | | September 30, | |
| | 2018 | 2017 | 2018 | 2017 |
| Net revenue | \$1,705,645 | \$1,198,198 | \$4,765,170 | \$3,281,879 |
| Cost of goods sold | 1,312,875 | 917,889 | 3,663,569 | 2,495,221 |
| Gross profit | 392,770 | 280,309 | 1,101,601 | 786,658 |
| Operating expenses: | | | | |
| Customer service and merchant fees | 66,664 | 42,949 | 182,340 | 117,132 |
| Advertising | 202,587 | 141,714 | 541,815 | 384,220 |
| Selling, operations, technology, general and administrative | 268,785 | 169,603 | 721,120 | 453,021 |
| Total operating expenses | 538,036 | 354,266 | 1,445,275 | 954,373 |
| Loss from operations | (145,266) | (73,957) | (343,674) | (167,715) |
| Interest expense, net | (7,066) | (2,008) | (18,269) | (3,857) |
| Other income (expense), net | 1,054 | (227) | 2,661 | 400 |
| Loss before income taxes | (151,278) | (76,192) | (359,282) | (171,172) |
| Provision for income taxes | 448 | 237 | 953 | 671 |
| Net loss | \$(151,726) | \$(76,429) | \$(360,235) | \$(171,843) |
| Net loss per share, basic and diluted | \$(1.69) | \$(0.88) | \$(4.04) | \$(1.98) |
| Weighted average number of common stock outstanding used in computing per share amounts, basic and diluted | 89,792 | 87,283 | 89,144 | 86,679 |

The accompanying notes are an integral part of these Unaudited Consolidated and Condensed Financial Statements.

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WAYFAIR INC.

CONSOLIDATED AND CONDENSED STATEMENTS OF COMPREHENSIVE LOSS

(In thousands)

(Unaudited)

| | Three months ended | | Nine months ended | |
|--|--------------------|------------|-------------------|-------------|
| | September 30, | | September 30, | |
| | 2018 | 2017 | 2018 | 2017 |
| Net loss | \$(151,726) | \$(76,429) | \$(360,235) | \$(171,843) |
| Other comprehensive loss: | | | | |
| Foreign currency translation adjustments | (243) | (856) | 249 | (1,959) |
| Net unrealized gain (loss) on available-for-sale investments | 85 | (40) | 47 | 3 |
| Comprehensive loss | \$(151,884) | \$(77,325) | \$(359,939) | \$(173,799) |

The accompanying notes are an integral part of these Unaudited Consolidated and Condensed Financial Statements.

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WAYFAIR INC.

CONSOLIDATED AND CONDENSED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

| | Nine months ended September 30, | |
|---|------------------------------------|-------------|
| | 2018 | 2017 |
| Cash flows from operating activities | | |
| Net loss | \$(360,235) | \$(171,843) |
| Adjustments to reconcile net loss to net cash used in operating activities | | |
| Depreciation and amortization | 87,426 | 62,588 |
| Equity based compensation | 88,148 | 46,740 |
| Amortization of discount and issuance costs on convertible notes | 13,699 | 874 |
| Other non-cash adjustments | 177 | 913 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (3,157) | (8,697) |
| Inventories | (7,757) | (38) |
| Prepaid expenses and other current assets | (37,376) | (27,776) |
| Accounts payable and accrued expenses | 187,733 | 44,692 |
| Deferred revenue and other liabilities | 80,509 | 50,450 |
| Other assets | (6,836) | (1,148) |
| Net cash provided by (used in) operating activities | 42,331 | (3,245) |
| Cash flows from investing activities | | |
| Purchase of short-term and long-term investments | — | (47,639) |
| Sale and maturities of short-term investments | 45,955 | 60,540 |
| Purchase of property and equipment | (110,504) | (76,528) |
| Site and software development costs | (45,769) | (34,885) |
| Other investing activities | (399) | — |
| Net cash used in investing activities | (110,717) | (98,512) |
| Cash flows from financing activities | | |
| Proceeds from issuance of convertible notes, net of issuance costs | — | 420,449 |
| Premiums paid for capped call confirmations | — | (44,160) |
| Taxes paid related to net share settlement of equity awards | (1,097) | (1,277) |
| Net proceeds from exercise of stock options | 104 | 213 |
| Net cash provided by (used in) financing activities | (993) | 375,225 |
| Effect of exchange rate changes on cash and cash equivalents | (945) | 413 |
| Net decrease in cash and cash equivalents | (70,324) | 273,881 |
| Cash and cash equivalents | | |
| Beginning of period | 558,960 | 279,840 |
| End of period | \$488,636 | \$553,721 |
| Supplemental Cash Flow Information | | |
| Cash paid for interest on long-term debt | \$1,554 | \$— |
| Purchase of property and equipment included in accounts payable and accrued expenses and in other liabilities | \$10,520 | \$9,255 |
| Construction costs capitalized under finance lease obligation and other leases | \$64,408 | \$16,153 |

The accompanying notes are an integral part of these Unaudited Consolidated and Condensed Financial Statements.

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Notes to Consolidated and Condensed Financial Statements
(Unaudited)

1. Basis of Presentation

Wayfair Inc. (the "Company") is one of the world's largest online destinations for the home. Through its e-commerce business model, the Company offers visually inspired browsing, compelling merchandising, easy product discovery and attractive prices for over ten million products from over 10,000 suppliers.

The consolidated and condensed financial statements and other disclosures contained in this Quarterly Report on Form 10-Q are those of the Company. Prior period expenses recorded in "Merchandising, marketing and sales" and "Operations, technology, general and administrative" have been combined into "Selling, operations, technology, general and administrative" on the consolidated statements of operations to conform with current presentation.

The consolidated and condensed balance sheet data as of December 31, 2017 was derived from audited financial statements. The accompanying consolidated and condensed balance sheet as of September 30, 2018, the consolidated and condensed statements of operations, consolidated and condensed statements of comprehensive loss, and consolidated and condensed statements of cash flows for the periods ended September 30, 2018 and 2017 are unaudited. The unaudited interim financial statements have been prepared on the same basis as the audited consolidated financial statements and in the opinion of management, reflect all adjustments, consisting of only normal recurring adjustments, necessary for the fair statement of the Company's financial position as of September 30, 2018 and statements of operations, comprehensive loss, and cash flows for the periods ended September 30, 2018 and 2017. The financial data and the other information disclosed in these notes to the consolidated and condensed financial statements related to these periods are unaudited.

The consolidated and condensed statements of operations, comprehensive loss, and cash flows for the period ended September 30, 2018 are not necessarily indicative of the results of operations and cash flows that may be expected for the year ending December 31, 2018, or for any other period.

2. Summary of Significant Accounting Policies

The Company has identified the significant accounting policies that are critical to understanding its business and results of operations.

Revenue Recognition

The Company adopted ASU No. 2014-09, "Revenue from Contracts with Customers" ("ASU 2014-09") as of January 1, 2018. The Company primarily generates net revenue through product sales on its five distinct sites ("Direct Retail" net revenue) and through (i) product sales on websites operated by third parties and (ii) fees earned for media solutions (collectively, "Other" net revenue).

The Company recognizes net revenue on product sales through the Company's five distinct sites and third party operated websites using the gross method when the Company has concluded it controls the product before it is transferred to the customer. The Company controls products when it is the entity responsible for fulfilling the promise to the customer and takes responsibility for the acceptability of the goods, assumes inventory risk from shipment through the delivery date, has discretion in establishing prices, and selects the suppliers of products sold. The Company recognizes net revenue from sales of its products upon delivery to the customer. As the Company ships a large volume of packages through multiple carriers, actual delivery dates may not always be available and as such the Company estimates delivery dates based on historical data.

Net revenue from product sales includes shipping costs charged to the customer and is recorded net of taxes collected from customers, which are remitted to governmental authorities. Cash discounts and rebates earned by customers at the time of purchase are deducted from gross revenue in determining net revenue. Allowances for sales returns are estimated and recorded based on prior returns history, recent trends, and projections for returns on sales in the current period.

The Company also earns revenue through third-party advertisers that pay based on the number of advertisement related clicks, actions, or impressions for advertisements placed on the Company's sites. Revenue earned under these arrangements is included in net revenue and is recognized in the period in which the click, action, or impression occurs.

Net revenue from contracts with customers is disaggregated by Direct Retail and Other net revenue and by geographic region because this manner of disaggregation best depicts how the nature, amount, timing, and uncertainty of revenue and cash flows are affected by economic factors. Refer to Note 8, Segment and Geographic Information, for additional detail.

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The Company has three types of contractual liabilities: (i) cash collections from its customers prior to delivery of products purchased, which are initially recorded in "Deferred revenue," and are recognized as net revenue when the products are delivered, (ii) unredeemed gift cards and site credits, which are initially recorded in "Deferred revenue," and are recognized in the period they are redeemed. Subject to requirements to remit balances to governmental agencies, certain gift cards and site credits not expected to be redeemed, also known as "breakage," are recognized as net revenue based on the historical redemption pattern, which is substantially within twenty-four months from the date of issuance, and (iii) membership rewards redeemable for future purchases, which are earned by customers on purchases made with the Company's Wayfair branded, private label credit card, and are initially recorded in "Other current liabilities," and are recognized as net revenue when redeemed.

Contractual liabilities included in "Deferred revenue" and "Other current liabilities" in the consolidated and condensed balance sheets were \$133.4 million and \$2.7 million at September 30, 2018 and \$94.1 million and \$2.6 million at December 31, 2017, respectively. During the nine months ended September 30, 2018, the Company recognized \$76.6 million and \$2.2 million of net revenue included in "Deferred revenue" and "Other current liabilities," respectively, at December 31, 2017.

The Company adopted ASU 2014-09 using a modified retrospective approach and recognized a \$4.7 million cumulative-effect adjustment to reduce "Accumulated deficit" as of January 1, 2018. The cumulative-effect adjustment to "Accumulated deficit" was due to breakage of gift cards and site credits, to the extent there is no requirement for remitting balances to governmental agencies. Prior period balances were not retrospectively adjusted. The Company believes that other than the implementation of ASU 2014-09, there have been no significant changes during the nine months ended September 30, 2018 to the items disclosed in Note 2, Summary of Significant Accounting Policies, included in Part II, Item 8, Financial Statements and Supplementary Data, of the Company's Annual Report on Form 10-K for the year ended December 31, 2017.

3. Marketable Securities and Fair Value Measurements

Marketable Securities

As of September 30, 2018 and December 31, 2017, all of the Company's marketable securities were classified as available-for-sale and their estimated fair values were \$36.6 million and \$82.6 million, respectively. The Company periodically reviews its available-for-sale securities for other-than-temporary impairment. The Company considers factors such as the duration, severity and the reason for the decline in value, the potential recovery period, and its intent to sell. As of September 30, 2018, the Company's available-for-sale securities primarily consisted of corporate bonds and other government obligations that are priced at fair value. During the three and nine months ended September 30, 2018 and 2017, the Company did not recognize any other-than-temporary impairment losses. The maturities of the Company's long-term marketable securities generally range from one to two years. The cost basis of a marketable security sold is determined by the Company using the specific identification method. During the three and nine months ended September 30, 2018 and 2017, the Company did not have any realized gains or losses.

The following tables present details of the Company's marketable securities as of September 30, 2018 and December 31, 2017 (in thousands):

| | September 30, 2018 | | | |
|-----------------------|--------------------|------------------------------|-------------------------------|-------------------------|
| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
| Short-term: | | | | |
| Investment securities | \$30,142 | \$ | —\$ (86) | \$ 30,056 |
| Long-term: | | | | |
| Investment securities | 6,619 | — | (98) | 6,521 |
| Total | \$36,761 | \$ | —\$ (184) | \$ 36,577 |

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December 31, 2017

| | Amortized Cost | Gross Unrealized Gains | Gross Unrealized Losses | Estimated Fair Value |
|-----------------------|-------------------|------------------------------|-------------------------------|-------------------------|
| Short-term: | | | | |
| Investment securities | \$61,129 | \$ | —\$ (97) | \$ 61,032 |
| Long-term: | | | | |
| Investment securities | 21,695 | — | (134) | 21,561 |
| Total | \$82,824 | \$ | —\$ (231) | \$ 82,593 |

Fair Value Measurements

The Company's financial assets and liabilities are measured at fair value, which is defined 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 (exit price). The three levels of inputs used to measure fair value are as follows:

Level 1—Unadjusted quoted prices in active markets for identical assets or liabilities

Level 2—Unadjusted quoted prices in active markets for similar assets or liabilities, unadjusted quoted prices for identical or similar assets or liabilities in markets that are not active, or inputs other than quoted prices that are observable or can be corroborated by observable market data for substantially the full-term of the asset or liability

Level 3—Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the asset or liability

This hierarchy requires the Company to use observable market data, when available, and to minimize the use of unobservable inputs when determining fair value. The Company measures its cash equivalents and short-term and long-term investments at fair value. The Company classifies its cash equivalents and restricted cash within Level 1 because the Company values these investments using quoted market prices. The fair value of the Company's Level 1 financial assets is based on quoted market prices of the identical underlying security. The Company classifies short-term and long-term investments within Level 2 because unadjusted quoted prices for identical or similar assets in markets are not active. The Company does not have any assets or liabilities classified as Level 3 financial assets. The following tables set forth the fair value of the Company's financial assets measured at fair value on a recurring basis as of September 30, 2018 and December 31, 2017 based on the three-tier value hierarchy (in thousands):

| | September 30, 2018 | | | Total |
|------------------------------------|--------------------|----------|---------|------------|
| | Level 1 | Level 2 | Level 3 | |
| Cash equivalents: | | | | |
| Money market funds and other funds | \$412,083 | \$— | \$ | —\$412,083 |
| Short-term investments: | | | | |
| Investment securities | — | 30,056 | — | 30,056 |
| Other non-current assets: | | | | |
| Certificate of deposit | 5,000 | — | — | 5,000 |
| Long-term: | | | | |
| Investment securities | — | 6,521 | — | 6,521 |
| Total | \$417,083 | \$36,577 | \$ | —\$453,660 |

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| | December 31, 2017 | | | |
|---------------------------|-------------------|----------|---------|------------|
| | Level 1 | Level 2 | Level 3 | Total |
| Cash equivalents: | | | | |
| Money market funds | \$488,029 | \$— | \$ | —\$488,029 |
| Short-term investments: | | | | |
| Investment securities | — | 61,032 | — | 61,032 |
| Other non-current assets: | | | | |
| Certificate of deposit | 5,000 | — | — | 5,000 |
| Long-term: | | | | |
| Investment securities | — | 21,561 | — | 21,561 |
| Total | \$493,029 | \$82,593 | \$ | —\$575,622 |

4. Intangible Assets and Goodwill

The following table summarizes intangible assets as of September 30, 2018 and December 31, 2017 (in thousands):

| | Weighted - Average Amortization Period (Years) | September 30, 2018 | | |
|------------------------|--|-----------------------|--------------------------|----------------|
| | | Gross Carrying Amount | Accumulated Amortization | Net Book Value |
| Trademarks | 5 | \$1,900 | \$ (1,900) | \$ — |
| Technology | 3 | 1,678 | (1,053) | 625 |
| Customer relationships | 5 | 1,300 | (1,300) | — |
| Total | | \$4,878 | \$ (4,253) | \$ 625 |
| | Weighted - Average Amortization Period (Years) | December 31, 2017 | | |
| | | Gross Carrying Amount | Accumulated Amortization | Net Book Value |
| Trademarks | 5 | \$1,900 | \$ (1,678) | \$ 222 |
| Technology | 3 | 1,453 | (646) | 807 |
| Customer relationships | 5 | 1,300 | (1,148) | 152 |
| Total | | \$4,653 | \$ (3,472) | \$ 1,181 |

Amortization expense related to intangible assets was \$0.2 million and \$0.3 million for the three months ended September 30, 2018 and 2017, respectively, and \$0.8 million for the nine months ended September 30, 2018 and 2017.

Goodwill was \$2.1 million and \$1.9 million as of September 30, 2018 and December 31, 2017, respectively.

5. Property and Equipment, net

The following table summarizes property and equipment, net as of September 30, 2018 and December 31, 2017 (in thousands):

| | September 30, 2018 | December 31, 2017 |
|--|--------------------|-------------------|
| Furniture and computer equipment | \$305,913 | \$213,790 |
| Site and software development costs | 157,717 | 118,356 |
| Leasehold improvements | 102,871 | 82,614 |
| Construction in progress | 16,832 | 46,826 |
| Buildings (leased - Note 6) | 184,694 | 83,681 |
| | 768,027 | 545,267 |
| Less accumulated depreciation and amortization | (258,366) | (184,126) |
| Property and equipment, net | \$509,661 | \$361,141 |

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Property and equipment depreciation and amortization expense was \$32.4 million and \$22.6 million for the three months ended September 30, 2018 and 2017, respectively, and \$86.6 million and \$61.7 million for the nine months ended September 30, 2018 and 2017, respectively.

6. Commitments and Contingencies

Leases

The Company leases office and warehouse spaces under non-cancelable leases. These leases expire at various dates through 2031 and include discounted rental periods and fixed escalation clauses, which are amortized straight-line over the terms of the lease. Rent expense under operating leases was \$16.9 million and \$10.6 million in the three months ended September 30, 2018 and 2017, respectively, and \$45.8 million and \$33.3 million in the nine months ended September 30, 2018 and 2017, respectively. The Company has issued letters of credit for approximately \$26.9 million and \$15.3 million as security for these lease agreements as of September 30, 2018 and December 31, 2017, respectively.

As of December 31, 2017, the future minimum rental commitments under non-cancelable leases with initial or remaining terms in excess of one year totaled \$783.7 million. Subsequent to December 31, 2017, the Company entered into additional non-cancelable leases in the United States ("U.S.") with initial or remaining terms in excess of one year with total future minimum lease commitments of \$231.8 million. Future lease payments have not been reduced by minimum sublease rentals of \$5.3 million due to the Company in the future under non-cancelable subleases through 2020.

The Company establishes assets and liabilities for the estimated construction costs incurred under lease arrangements where the Company is considered the owner for accounting purposes only, or build-to-suit leases, to the extent the Company is involved in the construction of structural improvements or takes construction risk prior to commencement of a lease. Upon occupancy of facilities under build-to-suit leases, the Company assesses whether these arrangements qualify for sales recognition under the sale-leaseback accounting guidance. If the Company continues to be the deemed owner, the facilities are accounted for as financing leases.

The construction of one warehouse lease arrangement was completed in the three months ended June 30, 2018, and because the Company had a letter of credit of \$2.5 million, the Company did not meet the sale-leaseback criteria for derecognition of the building asset and liability. The construction of a second and third warehouse lease arrangement was completed in the three months ended September 30, 2018 and because in both lease arrangements the Company provided non-recourse financing to the lessor, the Company did not meet the sale-leaseback criteria for derecognition of the building asset and liability.

Accordingly, these leases were accounted for as financing obligations and \$101.0 million was recorded in "Lease financing obligation, net of current portion" and "Property and equipment, net" in the Company's unaudited consolidated and condensed balance sheet as of September 30, 2018. The monthly rent payments made to the lessor under the lease agreement are recorded in the Company's financial statements as land lease expense and principal and interest on the financing obligation. Interest expense on the lease financing obligation reflects the portion of the Company's monthly lease payments that is allocated to interest expense. For the three and nine months ended September 30, 2018, land lease expense was \$0.7 million and \$2.1 million, respectively, and interest expense on lease financing obligations was \$3.5 million and \$8.0 million, respectively. As of September 30, 2018, future minimum commitments related to the financing obligations were \$20.2 million and \$76.2 million for principal and interest, respectively, through September 30, 2023.

Collection of Sales or Other Similar Taxes

The Company has historically collected and remitted sales tax based on the locations of its physical operations. On June 21, 2018, the U.S. Supreme Court rendered a 5-4 majority decision in *South Dakota v. Wayfair Inc.*, 17-494. Among other things, the Court held that a state may require an out-of-state seller with no physical presence in the state to collect and remit sales taxes on goods the seller ships to consumers in the state, overturning existing court precedent. Several states and other taxing jurisdictions have presented, or indicated that they may present, the Company with sales tax assessments. The aggregate assessments received as of September 30, 2018 are not material to the Company's business and the Company does not expect the Court's decision to have a significant impact on its business.

Legal Matters

On June 21, 2018, the U.S. Supreme Court rendered a 5-4 majority decision in *South Dakota v. Wayfair Inc.*, 17-494. Among other things, the Court held that a state may require an out-of-state seller with no physical presence in the state to collect and remit sales taxes on goods the seller ships to consumers in the state, overturning existing court precedent. See Collection of Sales or Other Similar Taxes above.

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From time to time the Company is involved in claims that arise during the ordinary course of business. Although the results of litigation and claims cannot be predicted with certainty, the Company does not currently believe that the outcome of any of these other legal matters will have a material adverse effect on the Company's results of operation or financial condition. Regardless of the outcome, litigation can be costly and time consuming, as it can divert management's attention from important business matters and initiatives, negatively impacting the Company's overall operations. In addition, the Company may also find itself at greater risk to outside party claims as it increases its operations in jurisdictions where the laws with respect to the potential liability of online retailers are uncertain, unfavorable, or unclear.

7. Equity-Based Compensation

The board of directors of the Company (the "Board") adopted the 2014 Incentive Award Plan ("2014 Plan") to grant cash and equity incentive awards to eligible participants in order to attract, motivate and retain talent. The 2014 Plan is administered by the Board with respect to awards to non-employee directors and by the compensation committee of the Board with respect to other participants and provides for the issuance of stock options, SARs, restricted stock, restricted stock units ("RSUs"), performance shares, stock payments, cash payments, dividend awards and other incentives. Prior to the adoption of the 2014 Plan, Wayfair LLC issued certain equity awards pursuant to the Wayfair LLC Amended and Restated Common Unit Plan (the "2010 Plan"), which was administered by the board of directors of Wayfair LLC. Awards issued under the 2010 Plan that remain outstanding currently represent Class A or Class B common stock of the Company.

8,603,066 shares of Class A common stock were initially available for issuance under awards granted pursuant to the 2014 Plan. The 2014 Plan also contains an evergreen provision whereby the shares available for future grant are increased on the first day of each calendar year beginning January 1, 2016 and ending on and including January 1, 2024. As of January 1, 2018, 8,016,850 shares of Class A common stock were available for future grant under the 2014 Plan. Shares or RSUs forfeited, withheld for minimum statutory tax obligations, and unexercised stock option lapses from the 2010 and 2014 Plans are available for future grant under the 2014 Plan.

The following table presents activity relating to stock options for the nine months ended September 30, 2018:

| | Options | Weighted-Average Exercise Price | Weighted-Average Remaining Contractual Term (Years) |
|---|-----------|---------------------------------|---|
| Outstanding at December 31, 2017 | 126,383 | \$ 3.02 | 3.5 |
| Options exercised | (34,981) | \$ 2.97 | |
| Outstanding and exercisable at September 30, 2018 | 91,402 | \$ 3.04 | 2.7 |

Intrinsic value of stock options exercised was \$3.2 million for the nine months ended September 30, 2018. Aggregate intrinsic value of stock options outstanding and currently exercisable is \$13.2 million. All stock options were fully vested at September 30, 2018.

The following table presents activity relating to restricted common stock for the nine months ended September 30, 2018:

| | Shares | Weighted-Average Grant Date Fair Value |
|--|--------|--|
| Unvested at December 31, 2017 | 40,000 | \$ 44.34 |
| Unvested and expected to vest in the future as of September 30, 2018 | 40,000 | \$ 44.34 |

Aggregate intrinsic value of unvested restricted common stock is \$5.9 million as of September 30, 2018.

Unrecognized equity based compensation expense related to unvested restricted common stock is \$3.7 million with a weighted average remaining vesting term of 0.8 years as of September 30, 2018.

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The following table presents activity relating to RSUs for the nine months ended September 30, 2018:

| | Shares | Weighted-Average Grant Date Fair Value |
|---|-------------|--|
| Outstanding at December 31, 2017 | 6,853,606 | \$ 46.28 |
| RSUs granted | 3,209,887 | \$ 89.87 |
| RSUs vested | (1,911,629) | \$ 44.84 |
| RSUs forfeited/canceled | (935,196) | \$ 53.19 |
| Outstanding and expected to vest in the future as of September 30, 2018 | 7,216,668 | \$ 65.30 |

The intrinsic value of RSUs vested was \$189.7 million for the nine months ended September 30, 2018. Aggregate intrinsic value of RSUs unvested is \$1,065.7 million as of September 30, 2018. Unrecognized equity based compensation expense related to outstanding RSUs is \$433.4 million with a weighted average remaining vesting term of 1.6 years at September 30, 2018.

8. Segment and Geographic Information

Operating segments are defined as components of an enterprise for which separate financial information is available that is evaluated on a regular basis by the Chief Operating Decision Maker ("CODM") in deciding how to allocate resources to an individual segment and in assessing performance. The Company's CODM is its Chief Executive Officer.

The Company's operating and reportable segments are U.S. and International. These segments reflect the way the CODM allocates resources and evaluates financial performance, which is based upon each segment's Adjusted EBITDA. Adjusted EBITDA is defined as loss before depreciation and amortization, equity-based compensation and related taxes, interest and other income and expense, provision for income taxes, and non-recurring items. These charges are excluded from evaluation of segment performance because it facilitates reportable segment performance comparisons on a period-to-period basis.

The Company allocates certain operating expenses to the operating and reportable segments, including "Customer service and merchant fees" and "Selling, operations, technology, general and administrative" based on the usage and relative contribution provided to the segments. It excludes from the allocations certain operating expense lines, including "Depreciation and amortization," "Equity based compensation and related taxes," "Interest expense, net," "Other (income) expense, net," and "Provision for income taxes." There are no revenue transactions between the Company's reportable segments.

U.S.

The U.S. segment primarily consists of amounts earned through product sales through the Company's five distinct sites in the U.S. and through websites operated by third parties in the U.S.

International

The International segment primarily consists of amounts earned through product sales through the Company's international sites.

Revenue from external customers for each group of similar products and services are not reported to the CODM. Separate identification of this information for purposes of segment disclosure is impractical, as it is not readily available and the cost to develop it would be excessive. No individual country outside of the U.S. provided greater than 10% of total revenue.

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The following tables present Direct Retail and Other net revenues and Adjusted EBITDA attributable to the Company's reportable segments for the periods presented (in thousands):

| | Three months ended | | Nine months ended | |
|---|--------------------|-------------|--------------------|-------------------|
| | September 30, | | September 30, | |
| | 2018 | 2017 | 2018 | 2017 |
| U.S. Direct Retail | \$1,460,056 | \$1,033,669 | \$4,043,270 | \$2,847,898 |
| U.S. Other | 13,189 | 16,975 | 42,903 | 57,843 |
| U.S. segment net revenue | 1,473,245 | 1,050,644 | 4,086,173 | 2,905,741 |
| International Direct Retail | 232,400 | 147,554 | 678,997 | 376,138 |
| International segment net revenue | 232,400 | 147,554 | 678,997 | 376,138 |
| Total net revenue | \$1,705,645 | \$1,198,198 | \$4,765,170 | \$3,281,879 |
| | | | Three months ended | Nine months ended |
| | | | September 30, | September 30, |
| | | | 2018 | 2017 |
| Adjusted EBITDA: | | | | |
| U.S. | \$(26,036) | \$4,531 | \$(26,774) | \$28,684 |
| International | (50,369) | (27,203) | (134,400) | (74,498) |
| Total reportable segments Adjusted EBITDA | (76,405) | (22,672) | (161,174) | (45,814) |
| Less: reconciling items (1) | (75,321) | (53,757) | (199,061) | (126,029) |
| Net loss | \$(151,726) | \$(76,429) | \$(360,235) | \$(171,843) |

(1) Adjustments are made to reconcile total reportable segments Adjusted EBITDA to consolidated net loss including the following (in thousands):

| | Three months | | Nine months ended | |
|---|-----------------|----------|-------------------|-----------|
| | ended September | | September 30, | |
| | 2018 | 2017 | 2018 | 2017 |
| Depreciation and amortization (1) | \$32,544 | \$22,913 | \$87,426 | \$62,588 |
| Equity based compensation and related taxes | 36,317 | 19,598 | 95,074 | 50,539 |
| Interest expense, net | 7,066 | 2,008 | 18,269 | 3,857 |
| Other (income) expense, net | (1,054) | 227 | (2,661) | (400) |
| Provision for income taxes | 448 | 237 | 953 | 671 |
| Other (1) | — | 8,774 | — | 8,774 |
| Total reconciling items | \$75,321 | \$53,757 | \$199,061 | \$126,029 |

(1) The Company recorded \$9.6 million of one-time charges in the three and nine months ended September 30, 2017 in "Selling, operations, technology, general and administrative" in the unaudited consolidated and condensed statements of operations related to a warehouse the Company vacated in July 2017. Of the \$9.6 million charges, \$8.8 million was included in "Other" and related primarily to the excess of the Company's estimated future remaining lease commitments through 2023 over its expected sublease income over the same period, and \$0.8 million was included in "Depreciation and amortization" related to accelerated depreciation of leasehold improvements in the warehouse.

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The following table presents the activity related to the Company's net revenue from Direct Retail sales derived through the Company's sites and Other sales derived through websites operated by third parties and fees from our media solutions business (in thousands):

| | Three months ended | | Nine months ended | |
|---------------|--------------------|-------------|-------------------|-------------|
| | September 30, | | September 30, | |
| | 2018 | 2017 | 2018 | 2017 |
| Net revenue | | | | |
| Direct Retail | \$1,692,456 | \$1,181,223 | \$4,722,267 | \$3,224,036 |
| Other | 13,189 | 16,975 | 42,903 | 57,843 |
| Net revenue | \$1,705,645 | \$1,198,198 | \$4,765,170 | \$3,281,879 |

The following table presents long-lived assets by segment (in thousands):

| | September 30, | December 31, |
|------------------------------|---------------|--------------|
| | 2018 | 2017 |
| Geographic long-lived assets | | |
| U.S. | \$494,713 | \$353,414 |
| International | 14,948 | 7,727 |
| Total | \$509,661 | \$361,141 |

9. Income Taxes

Income tax expense was \$0.4 million and \$0.2 million for the three months ended September 30, 2018 and 2017, respectively, and \$1.0 million and \$0.7 million for the nine months ended September 30, 2018 and 2017, respectively. The income tax expense recorded in the three and nine months ended September 30, 2018 and 2017 is primarily related to income earned in certain foreign jurisdictions and U.S. state income taxes.

Deferred income taxes reflect the impact of temporary differences between the amounts of assets and liabilities for financial reporting purposes and such amounts as measured by tax laws. The Company has deferred tax assets related to its net operating loss carryforwards accumulated since the fourth quarter of 2014 and related to net operating loss carryforwards of certain of its foreign subsidiaries. A valuation allowance against net deferred tax assets is required if, based upon the available evidence, it is more likely than not that some or all of the deferred tax assets will not be realized. The Company reassesses the valuation allowance on a quarterly basis and has provided a valuation allowance on substantially all of its worldwide net deferred tax assets.

The Company had no material unrecognized tax benefits as of September 30, 2018 and December 31, 2017. The Company's policy is to recognize interest and penalties related to unrecognized tax benefits as a component of income tax expense.

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10. Stockholders' Equity

Preferred Stock

The Company authorized 10,000,000 shares of undesignated preferred stock, \$0.001 par value per share, for future issuance. As of September 30, 2018, the Company had no shares of undesignated preferred stock issued or outstanding.

Common Stock

The Company authorized 500,000,000 shares of Class A common stock, \$0.001 par value per share, and 164,000,000 shares of Class B common stock, \$0.001 par value per share, of which 61,400,416 and 57,398,983 shares of Class A common stock and 28,726,124 and 30,809,627 shares of Class B common stock were outstanding as of September 30, 2018 and December 31, 2017, respectively. The rights of the holders of Class A common stock and Class B common stock are identical, except with respect to voting and conversion rights. Each share of Class A common stock is entitled to one vote per share and each share of Class B common stock is entitled to ten votes per share. Each share of Class B common stock may be converted into one share of Class A common stock at the option of its holder and will be automatically converted into one share of Class A common stock upon transfer thereof, subject to certain exceptions. In addition, upon the date on which the outstanding shares of Class B common stock represent less than 10% of the aggregate number of shares of the then outstanding Class A common stock and Class B common stock, or in the event of the affirmative vote or written consent of holders of at least 66 2/3% of the outstanding shares of Class B common stock, all outstanding shares of Class B common stock shall convert automatically into Class A common stock. Subject to preferences that may apply to any shares of preferred stock outstanding at the time, the holders of common stock are entitled to receive dividends out of funds legally available if the Board, in its discretion, determines to issue dividends and then only at the times and in the amounts that the Board may determine. Since the Company's initial public offering through September 30, 2018, 51,192,113 shares of Class B common stock were converted to Class A common stock.

11. Credit Agreement

On February 22, 2017, the Company entered into a \$40 million credit card program and a credit agreement consisting of a \$100 million secured revolving credit facility (the "Revolver") with Citibank, N.A. ("Citibank"). The Citibank credit facility replaced the Company's existing credit facility with Bank of America, N.A., which was terminated on February 22, 2017. On September 11, 2017, the Citibank credit agreement was amended with a new letter of credit sublimit and to make clarifying edits to the mandatory prepayment provisions of the credit agreement. On April 12, 2018, the Citibank credit agreement was amended further, including, among other changes: (i) to increase the letter of credit sublimit to \$65 million and (ii) to modify certain baskets in the exceptions to the negative covenants, including, without limitation, the restricted payments, investments and indebtedness covenants.

As amended, the Revolver has a \$65 million letter of credit sublimit and a \$10 million swing line sublimit, and a final maturity date of February 21, 2020. Wayfair LLC is the borrower (the "Borrower") under the Citibank credit agreement. Subject to certain conditions, the Borrower has the right to increase the Revolver by \$25 million. Borrowings under the Revolver will bear interest through maturity at a variable rate based upon, at the Borrower's option, either the Eurodollar rate or the base rate (which is the highest of (x) Citibank's prime rate, (y) one-half of 1.00% in excess of the federal funds effective rate, and (z) 1.00% in excess of the one-month Eurodollar rate), plus, in each case an applicable margin. From closing until September 30, 2019, the applicable margin for Eurodollar rate loans is 1.75% per annum and the applicable margin for base rate loans is 0.75% per annum. After September 30, 2019, the applicable margin is subject to specified changes depending on the applicable consolidated leverage ratio. Any amounts outstanding under the Revolver are due at maturity. In addition, subject to the terms and conditions set forth in the credit agreement, the Borrower is required to make certain mandatory prepayments prior to maturity. The Citibank credit agreement contains affirmative and negative covenants customarily applicable to senior secured credit facilities, including covenants that, among other things, will limit or restrict the ability of the Company and its subsidiaries, subject to negotiated exceptions, to incur additional indebtedness and additional liens on their assets, engage in mergers or acquisitions or dispose of assets, pay dividends or make other distributions, voluntarily prepay other indebtedness, enter into transactions with affiliated persons, make investments, and change the nature of their businesses. In addition, the Citibank credit agreement requires the Company to maintain certain financial ratios. As of

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September 30, 2018, the Company was in compliance with its covenants under the Revolver. The Company did not borrow any amounts under the Revolver during the nine months ended September 30, 2018 and the year ended December 31, 2017.

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12. Convertible Debt

On September 15, 2017, the Company issued \$431.25 million aggregate principal amount of 0.375% Convertible Senior Notes due 2022 (the "Notes"), which includes the exercise in full of the \$56.25 million over-allotment option, to Citigroup Global Markets Inc. and Goldman Sachs & Co. LLC as the initial purchasers of the Notes (the "Initial Purchasers").

The net proceeds from the sale of the Notes were approximately \$420.4 million, after deducting the Initial Purchasers' discounts and the estimated offering expenses payable by the Company. The Company used approximately \$44.2 million of the net proceeds from the offering to pay the cost of the capped call transactions, as further described below, with three financial institutions (the "Option Counterparties"). The Company intends to use the remainder of the net proceeds for working capital and general corporate purposes.

The Notes were issued pursuant to an indenture, dated September 15, 2017 (the "Indenture"), between the Company and U.S. Bank National Association, as trustee. The Company will pay interest on the Notes semiannually in arrears at a rate of 0.375% per annum on March 1 and September 1 of each year commencing on March 1, 2018. The Notes are convertible based upon an initial conversion rate of 9.61 shares of the Company's Class A common stock per \$1,000 principal amount of Notes (equivalent to a conversion price of approximately \$104.06 per share of the Company's Class A common stock). The conversion rate will be subject to adjustment upon the occurrence of certain specified events, including certain distributions and dividends to all or substantially all of the holders of the Company's Class A common stock, but will not be adjusted for accrued and unpaid interest. The Company will settle any conversions of the Notes in cash, shares of the Company's Class A common stock or a combination thereof, with the form of consideration determined at the Company's election.

The Notes will mature on September 1, 2022, unless earlier purchased, redeemed or converted. Prior to June 1, 2022, holders may convert all or a portion of their Notes only under the following circumstances: (1) during any calendar quarter commencing after the calendar quarter ending on December 31, 2017 (and only during such calendar quarter), if the last reported sale price of the Company's Class A common stock for at least 20 trading days (whether or not consecutive) during a period of 30 consecutive trading days ending on, and including, the last trading day of the immediately preceding calendar quarter is greater than or equal to 130% of the conversion price on each applicable trading day; (2) during the 5 business day period after any 10 consecutive trading day period (the "measurement period") in which the trading price per \$1,000 principal amount of Notes for each trading day of the measurement period was less than 98% of the product of the last reported sale price of the Company's Class A common stock and the conversion rate on each such trading day; (3) with respect to any Notes called for redemption by the Company, at any time prior to the close of business on the second scheduled trading day immediately preceding the redemption date; or (4) upon the occurrence of specified corporate events. On and after June 1, 2022 until the close of business on the second scheduled trading day immediately preceding the maturity date, holders may convert their Notes at any time, regardless of the foregoing circumstances.

The Company may not redeem the Notes prior to September 8, 2020. On or after September 8, 2020, the Company may redeem for cash all or part of the Notes if the last reported sale price of the Company's Class A common stock equals or exceeds 130% of the conversion price then in effect for at least 20 trading days (whether or not consecutive), including at least one of the five trading days immediately preceding the date on which the Company provides notice of redemption, during any 30 consecutive trading days ending on, and including the trading day immediately preceding the date on which the Company provides notice of the redemption. The redemption price will be 100% of the principal amount of the Notes to be redeemed, plus accrued and unpaid interest, if any.

Upon the occurrence of a fundamental change (as defined in the Indenture), holders may require the Company to repurchase all or a portion of their Notes for cash at a price equal to 100% of the principal amount of the Notes to be repurchased plus any accrued but unpaid interest to, but excluding, the fundamental change repurchase date. Holders of Notes who convert their Notes in connection with a notice of redemption or a make-whole fundamental change (each as defined in the Indenture) may be entitled to a premium in the form of an increase in the conversion rate of the Notes.

The Indenture contains customary terms and covenants, including that upon certain events of default occurring and continuing, either the Trustee or the holders of not less than 25% in aggregate principal amount of the Notes then

outstanding may declare the entire principal amount of all the Notes plus accrued interest, if any, to be immediately due and payable.

The Notes are general unsecured obligations of the Company. The Notes rank senior in right of payment to any of the Company's future indebtedness that is expressly subordinated in right of payment to the Notes; rank equal in right of payment to the Company's existing and future unsecured indebtedness that is not so subordinated; are effectively subordinated in right of payment to any of the Company's secured indebtedness to the extent of the value of the assets securing such indebtedness; and are structurally subordinated to all existing and future indebtedness and liabilities of the Company's subsidiaries.

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In accounting for the issuance of the Notes, the Company separated the Notes into liability and equity components. The carrying amount of the liability component was calculated by measuring the fair value of a similar liability that does not have an associated convertible feature. The carrying amount of the equity component, representing the conversion option, which does not meet the criteria for separate accounting as a derivative as it is indexed to the Company's own stock, was determined by deducting the fair value of the liability component from the par value of the Notes. The difference between the principal amount of the Notes and the liability component represents the debt discount, which is recorded as a direct deduction from the related debt liability in the consolidated and condensed balance sheet and amortized to interest expense using the effective interest method over the term of the Notes. The equity component of the Notes of approximately \$95.8 million is included in additional paid-in capital in the consolidated and condensed balance sheet and is not remeasured as long as it continues to meet the conditions for equity classification. The Company allocated transaction costs related to the Notes using the same proportions as the proceeds from the Notes. Transaction costs attributable to the liability component were recorded as a direct deduction from the related debt liability in the consolidated and condensed balance sheet and amortized to interest expense over the term of the Notes, and transaction costs attributable to the equity component were netted with the equity component in shareholders' equity.

Interest expense related to the Notes was \$5.2 million and \$0.9 million for the three months ended September 30, 2018 and 2017, respectively, and \$15.3 million and \$0.9 million for the nine months ended September 30, 2018 and 2017, respectively. Interest expense is comprised of the amortization of debt discount and debt issuance costs and the contractual coupon interest.

The estimated fair value of the Notes was \$646.1 million as of September 30, 2018. The estimated fair value of the Notes was determined through consideration of quoted market prices. The fair value is classified as Level 2, as defined in Note 3, Marketable Securities and Fair Value Measurements.

On September 11, 2017, the Company entered into privately negotiated capped call transactions (the "Base Capped Call Transactions") with the Option Counterparties and, in connection with the exercise in full of the over-allotment option by the Initial Purchasers, on September 14, 2017 entered into additional capped call transactions (such additional capped call transactions, the "Additional Capped Call Transactions" and, together with the Base Capped Call Transactions, the "Capped Call Transactions") with the Option Counterparties. The Capped Call Transactions are expected generally to reduce the potential dilution and/or offset the cash payments the Company is required to make in excess of the principal amount of the Notes upon conversion of the Notes in the event that the market price per share of the Company's Class A common stock is greater than the strike price of the Capped Call Transactions (which initially corresponds to the initial conversion price of the Notes and is subject to certain adjustments under the terms of the Capped Call Transactions), with such reduction and/or offset subject to a cap based on the cap price of the Capped Call Transactions. The Capped Call Transactions have an initial cap price of \$154.16 per share of the Company's Class A common stock, which represents a premium of 100% over the last reported sale price of the Company's Class A common stock on September 11, 2017, and is subject to certain adjustments under the terms of the Capped Call Transactions. Collectively, the Capped Call Transactions cover, initially, the number of shares of the Company's Class A common stock underlying the Notes, subject to anti-dilution adjustments substantially similar to those applicable to the Notes.

The Capped Call Transactions are separate transactions, in each case, entered into by the Company with the Option Counterparties, and are not part of the terms of the Notes and will not affect any holder's rights under the Notes. Holders of the Notes will not have any rights with respect to the Capped Call Transactions. The Capped Call Transactions do not meet the criteria for separate accounting as a derivative as they are indexed to the Company's stock. The premiums paid for the Capped Call Transactions have been included as a net reduction to additional paid-in capital within shareholders' equity.

13. Net Loss per Share

Basic and diluted net loss per share is presented using the two-class method required for participating securities: Class A and Class B common stock. The rights of the holders of Class A and Class B common stock are identical, except with respect to voting and conversion. For more information on the rights of Class A and Class B common stockholders, see Note 10, Stockholders' Equity (Deficit).

Basic net loss per share is computed using the weighted-average number of shares of common stock outstanding during the period. Diluted net loss per share is computed using the weighted-average number of shares of common stock and, if dilutive, common stock equivalents outstanding during the period. The Company's common stock equivalents consist of shares issuable upon the release of restricted stock units, and to a lesser extent, the incremental shares of common stock issuable upon the exercise of stock options and unvested restricted stock. The dilutive effect of these common stock equivalents is reflected in diluted earnings per share by application of the treasury stock method. The Company's basic and diluted net loss per share are the same because the Company has generated net loss and common stock equivalents are excluded from diluted net loss per share because they have an antidilutive impact.

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The Company allocates undistributed earnings between the classes on a one-to-one basis when computing net loss per share. As a result, basic and diluted net loss per Class A and Class B shares are equivalent.

The following table presents the calculation of basic and diluted net loss per share (in thousands, except per share data):

| | Three months ended September 30, | | Nine months ended September 30, | |
|--|-------------------------------------|------------|------------------------------------|-------------|
| | 2018 | 2017 | 2018 | 2017 |
| Net loss | \$(151,726) | \$(76,429) | \$(360,235) | \$(171,843) |
| Weighted average common shares used for basic and diluted net loss per share computation | 89,792 | 87,283 | 89,144 | 86,679 |
| Net loss per common share: | | | | |
| Basic and Diluted | \$(1.69) | \$(0.88) | \$(4.04) | \$(1.98) |

Dilutive common stock equivalents, representing potentially dilutive common stock options, restricted stock and restricted stock units, of 7.3 million and 6.6 million for the three and nine months ended September 30, 2018 and 2017, respectively, were excluded from diluted earnings per share calculations for these periods because of their anti-dilutive effect. Furthermore, the shares of Class A common stock that would be issuable if the Company elects to settle the Notes in shares were excluded from the diluted earnings per share calculation (using the if-converted method) for the nine month period ended September 30, 2018 because their effect would have been anti-dilutive. The Company may settle the conversions of the Notes in cash, shares of the Company's Class A common stock or any combination thereof at its election. The number of shares of the Company's Class A common stock issuable at the conversion price of \$104.06 per share is expected to be 4.1 million shares, however the Capped Call Transactions are expected generally to reduce the potential dilution of the Company's Class A common stock upon any conversion of Notes and/or offset the cash payments the Company is required to make in excess of the principal amount of the Notes. Under the Capped Call Transactions, the number of shares of Class A common stock issuable at the conversion price of \$154.16 is expected to be 2.8 million shares. For more information on the Notes and the Capped Call Transactions, see Note 12, Convertible Debt.

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14. Recent Accounting Pronouncements

Leases

In February 2016, the FASB issued ASU No. 2016-02, "Leases" ("ASU 2016-02"). This ASU revises the accounting related to leases by requiring lessees to recognize a lease liability and a right-of-use asset for virtually all of their leases (other than leases that meet the definition of a short-term lease). The liability will be equal to the present value of lease payments. The asset will be based on the liability, subject to adjustment, such as for initial direct costs. For income statement purposes, a dual model was retained, requiring leases to be classified as either operating or finance leases. Operating leases will result in straight-line expense (similar to current operating leases) while finance leases will result in a front-loaded expense pattern (similar to current capital leases). The new lease guidance also simplifies the accounting for sale and leaseback transactions. This ASU is effective for annual reporting periods beginning after December 15, 2018 and early adoption is permitted. In July 2018, the FASB issued ASU No. 2018-11, "Leases", Targeted Improvements, which creates an optional transition expedient that allows an entity to apply the transition provisions of the new standard, including its disclosure requirements, at its adoption date instead of at the beginning of the earliest comparative period presented as originally required by FASB ASU No. 2016-02. The Company will adopt the new lease standard as of January 1, 2019 using the modified retrospective approach, applying the transition provisions of the new standard as of the adoption date.

In connection with the adoption of the new lease standard, the Company has completed scoping reviews and continues to make progress in its updating business processes, systems, accounting policies and internal controls.

Management is currently evaluating the impact of the adoption of this ASU on the Company's consolidated financial statements, and expects it will have a material impact on its consolidated financial statements, primarily the consolidated balance sheets and related disclosures. At this time, the Company is unable to reasonably estimate the expected increase in assets and liabilities on the consolidated balance sheets and related disclosures upon adoption.

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ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion of our financial condition and results of operations should be read in conjunction with the consolidated and condensed financial statements and the notes thereto 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 December 31, 2017. This discussion contains forward-looking statements that involve risks and uncertainties. As a result of many factors, such as those included in the Special Note Regarding Forward Looking Statements and in Part II, Item 1A, Risk Factors, of this Quarterly Report on Form 10-Q and in our Annual Report on Form 10-K for the year ended December 31, 2017, our actual results may differ materially from those anticipated in these forward-looking statements.

The following discussion includes financial information prepared in accordance with generally accepted accounting principles ("GAAP"), as well as certain adjusted or non-GAAP financial measures such as Adjusted EBITDA, non-GAAP diluted net loss per share and free cash flow. Generally, a non-GAAP financial measure is a numerical measure of financial performance, financial position or cash flows that excludes (or includes) amounts that are included in (or excluded from) the most directly comparable measure calculated and presented in accordance with GAAP. Management believes the use of these non-GAAP measures on a consolidated and reportable segment basis assists investors in understanding the ongoing operating performance of our business by presenting comparable financial results between periods. For more information on these non-GAAP financial measures, including reconciliations to the most directly comparable GAAP financial measures, see "Non-GAAP Financial Measures" below.

Unless the context requires otherwise, references in this Quarterly Report on Form 10-Q to "Wayfair," "the Company," "we," "us" or "our" refer to Wayfair Inc. and its consolidated subsidiaries.

Overview

We are one of the world's largest online destinations for the home. Through our e-commerce business model, we offer visually inspired browsing, compelling merchandising, easy product discovery and attractive prices for over ten million products from over 10,000 suppliers. Because of the large market opportunity we see in front of us, we are currently investing across our business, including investments to expand our international business, to build our proprietary logistics network and to continue developing various product categories.

Our operating and reportable segments are U.S. and International. The following table presents Direct Retail and Other net revenues attributable to the Company's reportable segments for the periods presented (in thousands):

| | Three months ended | | Nine months ended | |
|-----------------------------------|--------------------|-------------|-------------------|-------------|
| | September 30, | | September 30, | |
| | 2018 | 2017 | 2018 | 2017 |
| U.S. Direct Retail | \$1,460,056 | \$1,033,669 | \$4,043,270 | \$2,847,898 |
| U.S. Other | 13,189 | 16,975 | 42,903 | 57,843 |
| U.S. segment net revenue | 1,473,245 | 1,050,644 | 4,086,173 | 2,905,741 |
| International Direct Retail | 232,400 | 147,554 | 678,997 | 376,138 |
| International segment net revenue | 232,400 | 147,554 | 678,997 | 376,138 |
| Total net revenue | \$1,705,645 | \$1,198,198 | \$4,765,170 | \$3,281,879 |

For more information on our segments, see Note 8, Segment and Geographic Information, included in Part I, Item 1, Unaudited Consolidated and Condensed Financial Statements, of this Quarterly Report on Form 10-Q.

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Key Financial and Operating Metrics

We measure our business using both financial and operating metrics. Our free cash flow metric is measured on a consolidated basis. Our net revenue and Adjusted EBITDA metrics are measured on a consolidated and segment basis. See Note 8, Segment and Geographic Information, included in Part I, Item 1, Unaudited Consolidated and Condensed Financial Statements, of this Quarterly Report on Form 10-Q. All other key financial and operating metrics are derived and reported from our Direct Retail sales, which includes sales generated primarily through our five distinct sites. These metrics do not include net revenue derived from the websites operated by our retail partners and our media solutions business. We do not have access to certain customer level information on net revenue derived through our retail partners and therefore cannot measure or disclose it.

We use the following metrics to assess the near-term and longer-term performance of our overall business (in thousands, except LTM Net Revenue per Active Customer and Average Order Value):

| | Three months ended | | |
|--|--------------------|--------------|----------|
| | September 30, | | |
| | 2018 | 2017 | % Change |
| Consolidated Financial Metrics | | | |
| Net Revenue | \$1,705,645 | \$1,198,198 | 42.4 % |
| Adjusted EBITDA | \$(76,405) | \$(22,672) | |
| Free cash flow | \$(58,803) | \$(18,463) | |
| Direct Retail Financial and Operating Metrics | | | |
| Direct Retail Net Revenue | \$1,692,456 | \$1,181,223 | 43.3 % |
| Active Customers | 13,860 | 10,250 | 35.2 % |
| LTM Net Revenue per Active Customer | \$443 | \$408 | 8.6 % |
| Orders Delivered | 6,938 | 4,719 | 47.0 % |
| Average Order Value | \$244 | \$250 | (2.4)% |
| | Nine months ended | | |
| | September 30, | | |
| | 2018 | 2017 | % Change |
| Consolidated Financial Metrics | | | |
| Net Revenue | \$4,765,170 | \$3,281,879 | 45.2 % |
| Adjusted EBITDA | \$(161,174) | \$(45,814) | |
| Free cash flow | \$(113,942) | \$(114,658) | |
| Direct Retail Financial and Operating Metrics | | | |
| Direct Retail Net Revenue | \$4,722,267 | \$3,224,036 | 46.5 % |
| Active Customers | 13,860 | 10,250 | 35.2 % |
| LTM Net Revenue per Active Customer | \$443 | \$408 | 8.6 % |
| Orders Delivered | 19,278 | 13,209 | 45.9 % |
| Average Order Value | \$245 | \$244 | 0.4 % |

Non-GAAP Financial Measures

Adjusted EBITDA

To provide investors with additional information regarding our financial results, we have disclosed here and elsewhere in this Quarterly Report on Form 10-Q Adjusted EBITDA, a non-GAAP financial measure that we calculate as income (loss) before depreciation and amortization, equity-based compensation and related taxes, interest and other income and expense, provision for income taxes, and non-recurring items. We have provided a reconciliation below of Adjusted EBITDA to net loss, the most directly comparable GAAP financial measure.

We have included Adjusted EBITDA in this Quarterly Report on Form 10-Q because it is a key measure used by our management and board of directors to evaluate our operating performance, generate future operating plans, and make strategic decisions regarding the allocation of capital. In particular, the exclusion of certain expenses in calculating Adjusted EBITDA facilitates operating performance comparisons on a period-to-period basis. Accordingly, we

believe that Adjusted EBITDA provides useful information to investors and others in understanding and evaluating our operating results in the same manner as our management and board of directors.

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Adjusted EBITDA has limitations as an analytical tool, and you should not consider it in isolation or as a substitute for analysis of our results as reported under GAAP. Some of these limitations are:

Although depreciation and amortization are non-cash charges, the assets being depreciated and amortized may have to be replaced in the future, and Adjusted EBITDA does not reflect cash capital expenditure requirements for such replacements or for new capital expenditure requirements;

Adjusted EBITDA does not reflect equity based compensation and related taxes;

Adjusted EBITDA does not reflect changes in our working capital;

Adjusted EBITDA does not reflect income tax payments that may represent a reduction in cash available to us;

Adjusted EBITDA does not reflect depreciation and interest expenses associated with the lease financing obligation; and

Other companies, including companies in our industry, may calculate Adjusted EBITDA differently, which reduces its usefulness as a comparative measure.

Because of these limitations, you should consider Adjusted EBITDA alongside other financial performance measures, including various cash flow metrics, net loss and our other GAAP results.

The following table reflects the reconciliation of net loss to Adjusted EBITDA for each of the periods indicated (in thousands):

| | Three months ended | | Nine months ended | |
|---|--------------------|------------|-------------------|-------------|
| | September 30, | | September 30, | |
| | 2018 | 2017 | 2018 | 2017 |
| Reconciliation of Adjusted EBITDA | | | | |
| Net loss | \$(151,726) | \$(76,429) | \$(360,235) | \$(171,843) |
| Depreciation and amortization (1) | 32,544 | 22,913 | 87,426 | 62,588 |
| Equity based compensation and related taxes | 36,317 | 19,598 | 95,074 | 50,539 |
| Interest expense, net | 7,066 | 2,008 | 18,269 | 3,857 |
| Other (income) expense, net | (1,054) | 227 | (2,661) | (400) |
| Provision for income taxes | 448 | 237 | 953 | 671 |
| Other (1) | — | 8,774 | — | 8,774 |
| Adjusted EBITDA | \$(76,405) | \$(22,672) | \$(161,174) | \$(45,814) |

(1) We recorded \$9.6 million of one-time charges in the three and nine months ended September 30, 2017 in "Selling, operations, technology, general and administrative" in the unaudited consolidated and condensed statements of operations related to a warehouse we vacated in July 2017. Of the \$9.6 million charges, \$8.8 million was included in "Other" and related primarily to the excess of our estimated future remaining lease commitments through 2023 over our expected sublease income over the same period, and \$0.8 million was included in "Depreciation and amortization" related to accelerated depreciation of leasehold improvements in the warehouse.

Free Cash Flow

To provide investors with additional information regarding our financial results, we have also disclosed here and elsewhere in this Quarterly Report on Form 10-Q free cash flow, a non-GAAP financial measure that we calculate as net cash provided by (used in) operating activities less net cash used to purchase property and equipment and site and software development costs. We have provided a reconciliation below of free cash flow to net cash provided by (used in) operating activities, the most directly comparable GAAP financial measure.

We have included free cash flow in this Quarterly Report on Form 10-Q because it is an important indicator of our business performance as it measures the amount of cash we generate. Accordingly, we believe that free cash flow provides useful information to investors and others in understanding and evaluating our operating results in the same manner as our management.

Free cash flow has limitations as an analytical tool because it omits certain components of the cash flow statement and does not represent the residual cash flow available for discretionary expenditures. Further, other companies, including companies in our industry, may calculate free cash flow differently. Accordingly, you should not consider free cash flow in isolation or as a substitute for analysis of our results as reported under GAAP. Because of these limitations, you should consider

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free cash flow alongside other financial performance measures, including net cash provided by (used in) operating activities, capital expenditures and our other GAAP results.

The following table presents a reconciliation of free cash flow to net cash used in operating activities for each of the periods indicated (in thousands):

| | Three months ended | | Nine months ended | |
|---|--------------------|------------|-------------------|-------------|
| | September 30, | | September 30, | |
| | 2018 | 2017 | 2018 | 2017 |
| Net cash provided by (used in) operating activities | \$7,804 | \$24,752 | \$42,331 | \$(3,245) |
| Purchase of property and equipment | (49,411) | (30,980) | (110,504) | (76,528) |
| Site and software development costs | (17,196) | (12,235) | (45,769) | (34,885) |
| Free cash flow | \$(58,803) | \$(18,463) | \$(113,942) | \$(114,658) |

Key Operating Metrics (Direct Retail)**Active Customers**

As of the last date of each reported period, we determine our number of active customers by counting the total number of individual customers who have purchased at least once directly from our sites during the preceding twelve-month period. The change in active customers in a reported period captures both the inflow of new customers as well as the outflow of existing customers who have not made a purchase in the last twelve months. We view the number of active customers as a key indicator of our growth.

LTM Net Revenue Per Active Customer

We define LTM net revenue per active customer as our total net revenue derived from Direct Retail sales in the last twelve months divided by our total number of active customers for the same preceding twelve-month period. We view LTM net revenue per active customer as a key indicator of our customers' purchasing patterns, including their initial and repeat purchase behavior.

Orders Delivered

We define orders delivered as the total Direct Retail orders delivered in any period, inclusive of orders that may eventually be returned. As we ship a large volume of packages through multiple carriers, actual delivery dates may not always be available, and as such we estimate delivery dates based on historical data. We recognize net revenue when an order is delivered and therefore orders delivered, together with average order value, is an indicator of the net revenue we expect to recognize in a given period. We view orders delivered as a key indicator of our growth.

Average Order Value

We define average order value as total Direct Retail net revenue in a given period divided by the orders delivered in that period. We view average order value as a key indicator of the mix of products on our sites, the mix of offers and promotions and the purchasing behavior of our customers.

Factors Affecting our Performance

We believe that our performance and future success depend on a number of factors that present significant opportunities for us but also pose risks and challenges, including those set forth under Part II, Item 1A, Risk Factors, of this Quarterly Report on Form 10-Q and in our Annual Report on Form 10-K for the year ended December 31, 2017.

Components of Our Results of Operations**Net Revenue**

Net revenue consists primarily of sales of product from our sites and through the sites of our online retail partners and includes related shipping fees. We deduct cash discounts, allowances and estimated returns from gross revenue to determine net revenue. We recognize product revenue upon delivery to our customers. Net revenue is primarily driven by growth of new and active customers and the frequency with which customers purchase. The products offered on our sites are fulfilled with product we ship to our customers directly from our suppliers and, increasingly, from our CastleGate warehouses.

We also generate net revenue through third-party advertisers that pay us based on the number of advertisement related clicks, actions, or impressions for advertisements placed on our sites. Net revenue earned under these arrangements is included

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in net revenue and net revenue through our third-party advertisers is recognized in the period in which the click, action or impression occurs. This revenue has not been material to date.

Cost of Goods Sold

Cost of goods sold consists of the cost of product sold to customers, shipping and handling costs and shipping supplies and fulfillment costs. Fulfillment costs include costs incurred in operating and staffing the fulfillment centers, such as costs attributed to receiving, inspecting, picking, packaging and preparing customer orders for shipment. Cost of goods sold also includes direct and indirect labor costs, including equity-based compensation, for fulfillment center oversight, including payroll and related benefit costs. The increase in cost of goods sold is primarily driven by growth in orders delivered, the mix of the product available for sale on our sites and transportation costs related to delivering orders to our customers.

We earn rebates on our incentive programs with our suppliers. These rebates are earned upon shipment of goods. Amounts due from suppliers as a result of these rebate programs are included as a receivable and are reflected as a reduction of cost of goods sold on the consolidated and condensed statements of operations. We also perform logistics services for suppliers through our CastleGate solution, which are earned upon completion of preparing customer orders for shipment and are reflected as a reduction of cost of goods sold on the consolidated and condensed statements of operations. We expect cost of goods sold expenses to remain relatively stable as a percentage of net revenue but some fluctuations are expected due to the wide variety of products we sell.

Customer Service and Merchant Fees

Customer service and merchant fees consist of labor-related costs, including equity-based compensation, of our employees involved in customer service activities and merchant processing fees associated with customer payments made by credit cards and debit cards. Increases in our customer service and merchant fees are driven by the growth in our revenue and are expected to remain relatively consistent as a percentage of revenue.

Advertising

Advertising consists of direct response performance marketing costs, such as display advertising, paid search advertising, social media advertising, search engine optimization, comparison shopping engine advertising, television advertising, direct mail, catalog and print advertising. We expect advertising expense to continue to increase but decrease as a percentage of net revenue over time due to our increasing base of repeat customers.

Selling, Operations, Technology and General and Administrative

Selling, operations, technology, general and administrative expenses primarily include labor-related costs, including equity-based compensation, of our operations group, which includes our supply chain and logistics team, our technology team, which builds and supports our sites, category managers, buyers, site merchandisers, merchants, marketers and the team who executes our advertising strategy, and our corporate general and administrative team, which includes human resources, finance and accounting personnel. Also included are administrative and professional service fees including audit and legal fees, insurance and other corporate expenses, including depreciation and rent. We expect selling, operations, technology, general and administrative expenses will continue to increase as we grow our net revenue and operations.

Interest Expense, Net

Interest expense, net consists primarily of interest expense for the convertible debt and lease financing obligations, partially offset by interest income earned on cash, cash equivalents and short-term and long-term investments held by us.

Other Income, Net

Other income (expense), net consists primarily of foreign currency gains (losses).

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Results of Consolidated Operations (in thousands)

Comparison of the three months ended September 30, 2018 and 2017

Net revenue

| | Three months ended | | |
|---------------|--------------------|-------------|----------|
| | September 30, | | |
| | 2018 | 2017 | % Change |
| Direct Retail | \$1,692,456 | \$1,181,223 | 43.3 % |
| Other | 13,189 | 16,975 | (22.3)% |
| Net revenue | \$1,705,645 | \$1,198,198 | 42.4 % |

In the three months ended September 30, 2018, net revenue increased by \$507.4 million, or 42.4% compared to the same period in 2017, primarily as a result of an increase in Direct Retail net revenue. In the three months ended September 30, 2018, Direct Retail net revenue increased by \$511.2 million, or 43.3% compared to the same period in 2017, primarily due to sales to a larger customer base, as the number of active customers increased 35.2% as of September 30, 2018 compared to September 30, 2017. The \$3.8 million or 22.3% decrease in Other revenue in the three months ended September 30, 2018 as compared to the same period in 2017 was primarily due to decreased sales through our retail partners, as we continue to focus more on our Direct Retail business over time.

Cost of goods sold

| | Three months ended | | |
|--------------------------------|--------------------|-----------|----------|
| | September 30, | | |
| | 2018 | 2017 | % Change |
| Cost of goods sold | \$1,312,875 | \$917,889 | 43.0 % |
| As a percentage of net revenue | 77.0 | % 76.6 | % |

In the three months ended September 30, 2018, cost of goods sold increased by \$395.0 million, or 43.0%, compared to the same period in 2017. Of the increase in cost of goods sold, \$300.0 million was due to the increase in products sold to our larger customer base. In addition, shipping and fulfillment costs increased \$95.0 million as a result of the increase in products sold during the period. Cost of goods sold as a percentage of net revenue increased in the three months ended September 30, 2018 compared to the same period in 2017 as a result of the mix of the products sold.

Operating expenses

| | Three months ended | | |
|--|--------------------|-----------|----------|
| | September 30, | | |
| | 2018 | 2017 | % Change |
| Customer service and merchant fees (1) | \$66,664 | \$42,949 | 55.2 % |
| Advertising | 202,587 | 141,714 | 43.0 % |
| Selling, operations, technology, general and administrative | 268,785 | 169,603 | 58.5 % |
| | \$538,036 | \$354,266 | 51.9 % |
| As a percentage of net revenue: | | | |
| Customer service and merchant fees (1) | 3.9 | % 3.6 | % |
| Advertising | 11.9 | % 11.8 | % |
| Selling operations, technology, general and administrative (1) | 15.8 | % 14.2 | % |
| | 31.6 | % 29.6 | % |

(1) Includes equity-based compensation and related taxes as follows:

| | Three months ended | |
|--|--------------------|----------|
| | September 30, | |
| | 2018 | 2017 |
| Customer service and merchant fees | \$1,549 | \$636 |
| Selling operations, technology, general and administrative | \$34,041 | \$18,680 |

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The following table summarizes operating expenses as a percentage of net revenue, excluding equity-based compensation and related taxes:

| | Three months ended | |
|---|--------------------|--------|
| | September 30, | |
| | 2018 | 2017 |
| Customer service and merchant fees | 3.8 % | 3.5 % |
| Selling, operations, technology, general and administrative | 13.8 % | 12.6 % |

Excluding the impact of equity based compensation and related taxes, customer service costs and merchant processing fees increased by \$22.8 million in the three months ended September 30, 2018 compared to the same period in 2017, primarily due to the increase in net revenue during the three months ended September 30, 2018.

Our advertising expenses increased by \$60.9 million in the three months ended September 30, 2018 compared to the same period in 2017, primarily as a result of an increase in online and television advertising. Advertising was relatively consistent as a percentage of net revenue in the three months ended September 30, 2018 compared to the same period in 2017.

Excluding the impact of equity based compensation and related taxes, selling, operations, technology, general and administrative expense increased by \$83.8 million in the three months ended September 30, 2018 compared to the same period in 2017. As our revenue continues to grow, we have invested in headcount in both operations and technology to continue to deliver a great experience for our customers. The increase in operations, technology, general and administrative expense was primarily attributable to personnel costs, rent, information technology, and depreciation and amortization.

Comparison of the nine months ended September 30, 2018 and 2017

Net revenue

| | Nine months ended | | |
|---------------|-------------------|-------------|----------|
| | September 30, | | |
| | 2018 | 2017 | % Change |
| Direct Retail | \$4,722,267 | \$3,224,036 | 46.5 % |
| Other | 42,903 | 57,843 | (25.8)% |
| Net revenue | \$4,765,170 | \$3,281,879 | 45.2 % |

In the nine months ended September 30, 2018, net revenue increased by \$1,483.3 million, or 45.2% compared to the same period in 2017, primarily as a result of an increase in Direct Retail net revenue. In the nine months ended September 30, 2018, Direct Retail net revenue increased by \$1,498.2 million, or 46.5% compared to the same period in 2017, primarily due to sales to a larger customer base, as the number of active customers increased 35.2% as of September 30, 2018 compared to September 30, 2017. Additionally, LTM net revenue per active customer increased 8.6% as of September 30, 2018 compared to September 30, 2017. The \$14.9 million or 25.8% decrease in Other revenue in the nine months ended September 30, 2018 as compared to the same period in 2017 was primarily due to decreased sales through our retail partners, as we continue to focus more on our Direct Retail business over time.

Cost of goods sold

| | Nine months ended | | |
|--------------------------------|-------------------|-------------|----------|
| | September 30, | | |
| | 2018 | 2017 | % Change |
| Cost of goods sold | \$3,663,569 | \$2,495,221 | 46.8 % |
| As a percentage of net revenue | 76.9 % | 76.0 % | |

In the nine months ended September 30, 2018, cost of goods sold increased by \$1,168.3 million, or 46.8%, compared to the same period in 2017. Of the increase in cost of goods sold, \$891.3 million was due to the increase in products sold to our larger customer base. In addition, shipping and fulfillment costs increased \$277.0 million as a result of the increase in products sold during the period. Cost of goods sold as a percentage of net revenue increased in the nine months ended September 30, 2018 compared to the same period in 2017 as a result of changes in the mix of the products sold.

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Operating expenses

| | Nine months ended | | |
|---|-------------------|-----------|----------|
| | September 30, | | |
| | 2018 | 2017 | % Change |
| Customer service and merchant fees (1) | \$182,340 | \$117,132 | 55.7 % |
| Advertising | 541,815 | 384,220 | 41.0 % |
| Selling, operations, technology, general and administrative (1) | 721,120 | 453,021 | 59.2 % |
| Total operating expenses | \$1,445,275 | \$954,373 | 51.4 % |
| As a percentage of net revenue | | | |
| Customer service and merchant fees (1) | 3.8 | % 3.6 | % |
| Advertising | 11.4 | % 11.7 | % |
| Selling, operations, technology, general and administrative (1) | 15.1 | % 13.8 | % |
| | 30.3 | % 29.1 | % |

(1) Includes equity-based compensation and related taxes as follows:

| | Nine months | |
|---|---------------------|----------|
| | ended September 30, | |
| | 2018 | 2017 |
| Customer service and merchant fees | \$3,652 | \$1,866 |
| Selling, operations, technology, general and administrative | \$89,493 | \$48,041 |

The following table summarizes operating expenses as a percentage of net revenue, excluding equity-based compensation and related taxes:

| | Nine months | |
|---|---------------|--------|
| | ended | |
| | September 30, | |
| | 2018 | 2017 |
| Customer service and merchant fees | 3.7 % | 3.5 % |
| Selling, operations, technology, general and administrative | 13.3 % | 12.3 % |

Excluding the impact of equity based compensation and related taxes, customer service costs and merchant processing fees increased by \$63.4 million in the nine months ended September 30, 2018 compared to the same period in 2017, primarily due to the increase in net revenue during the nine months ended September 30, 2018.

Our advertising expenses increased by \$157.6 million in the nine months ended September 30, 2018 compared to the same period in 2017, primarily as a result of an increase in online and television advertising. Advertising decreased as a percentage of net revenue in the nine months ended September 30, 2018 compared to the same period in 2017 primarily due to increased leverage from our growing base of repeat customers, and television advertising expense not increasing at the same rate as revenue growth in the U.S., partially offset by advertising investments in Europe and Canada.

Excluding the impact of equity based compensation and related taxes, selling, operations, technology, general and administrative expense increased by \$226.6 million in the nine months ended September 30, 2018 compared to the same period in 2017. As our revenue continues to grow, we have invested in headcount in both operations and technology to continue to deliver a great experience for our customers. The increase in selling, operations, technology, general and administrative expense was primarily attributable to personnel costs, rent, information technology, and depreciation and amortization.

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Liquidity and Capital Resources

Sources of Liquidity

| | September 30, 2018 | December 31, 2017 |
|---------------------------|--------------------------|-------------------------|
| | (in thousands) | |
| Cash and cash equivalents | \$488,636 | \$558,960 |
| Short-term investments | \$30,056 | \$61,032 |
| Accounts receivable, net | \$41,013 | \$37,948 |
| Long-term investments | \$6,521 | \$21,561 |
| Working capital | \$(239,129) | \$77,065 |

Historical Cash Flows

| | Nine months ended September 30, 2018 | | 2017 |
|---|--|-------------|------|
| | (in thousands) | | |
| Net loss | \$(360,235) | \$(171,843) | |
| Net cash provided by (used in) operating activities | \$42,331 | \$(3,245) | |
| Net cash used in investing activities | \$(110,717) | \$(98,512) | |
| Net cash provided by (used in) financing activities | \$(993) | \$375,225 | |

At September 30, 2018, our principal source of liquidity was cash and cash equivalents and short- and long-term investments totaling \$525.2 million, which includes \$420.4 million of net proceeds from the issuance of our convertible notes in September 2017, partially offset by \$44.2 million in premiums paid at the same time for separate capped call transactions. We believe that our existing cash and cash equivalents and investments, together with cash generated from operations and the cash available under our revolving credit facility, will be sufficient to meet our anticipated cash needs for at least the foreseeable future. However, our liquidity assumptions may prove to be incorrect, and we could exhaust our available financial resources sooner than we currently expect. In addition, we may elect to raise additional funds at any time through equity, equity linked or debt financing arrangements.

Capital expenditures were 3.1% of net revenue for the year ended December 31, 2017, and related primarily to our ongoing investments in our technology infrastructure, and equipment purchases and improvements for leased warehouses within our expanding supply chain network. Capital expenditures were 3.9% of net revenue for the quarter ended September 30, 2018. For the three months ending December 31, 2018, we expect capital expenditures to be approximately 3.0% to 4.0% of net revenue as we continue to build out our logistics network.

Our future capital requirements and the adequacy of available funds will depend on many factors, including those described herein and in our other filings with the SEC, including those set forth under in Part II, Item 1A, Risk Factors, of this Quarterly Report on Form 10-Q and in our Annual Report on Form 10-K for the year ended December 31, 2017. We may not be able to secure additional financing to meet our operating requirements on acceptable terms, or at all.

Operating Activities

Cash flows in connection with operating activities consisted of net loss adjusted for certain non-cash items including depreciation and amortization, equity-based compensation, and certain other non-cash expenses, as well as the effect of changes in working capital and other activities. Operating cash flows can be volatile and are sensitive to many factors, including changes in working capital and our net loss.

Cash provided by operating activities in the nine months ended September 30, 2018 was \$42.3 million and was driven primarily by cash provided by operating assets and liabilities of \$213.1 million and the net impact of certain non-cash items including depreciation and amortization expense of \$87.4 million, equity based compensation of \$88.1 million, amortization of discount and issuance costs related to our convertible notes of \$13.7 million and other non-cash items of \$0.2 million, partially offset by net loss of \$360.2 million.

Cash used in operating activities in the nine months ended September 30, 2017 was \$3.2 million and was driven primarily by net loss of \$171.8 million, partially offset by cash provided by operating assets and liabilities of \$57.5 million and certain

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non-cash items including depreciation and amortization expense of \$62.6 million, equity based compensation of \$46.7 million, other non-cash items of \$0.9 million, and amortization of discount and issuance costs related to our convertible notes of \$0.9 million.

Investing Activities

Our primary investing activities consisted of purchases of property and equipment, particularly purchases of servers and networking equipment, investment in our sites and software development, purchases and disposal of short-term and long-term investments, and leasehold improvements for our facilities.

Cash used in investing activities in the nine months ended September 30, 2018 was \$110.7 million and was primarily driven by purchases of property and equipment of \$110.5 million and site, software development costs of \$45.8 million, and other investing activities of \$0.4 million, partially offset by net increase in the maturity of short-term investments of \$46.0 million.

Cash used in investing activities in the nine months ended September 30, 2017 was \$98.5 million and was primarily driven by purchases of property and equipment of \$76.5 million, purchases of short-term and long-term investments of \$47.6 million, and site and software development costs of \$34.9 million, partially offset by net increase in the maturity of short-term investments of \$60.5 million.

Financing Activities

Cash used in financing activities in the nine months ended September 30, 2018 was \$1.0 million and was primarily due to \$1.1 million statutory minimum taxes paid related to net share settlements of equity awards, partially offset by \$0.1 million net proceeds from exercise of stock options.

Cash provided by financing activities in the nine months ended September 30, 2017 was \$375.2 million and was primarily due to \$420.4 million of proceeds from the issuance of our 0.375% Convertible Senior Notes due 2022 (the "Notes") and \$0.2 million net proceeds from the exercise of stock options, partially offset by \$44.1 million in premiums paid for separate capped call transactions, and \$1.3 million statutory minimum taxes paid related to net share settlements of equity awards.

Stock Repurchase Program

On February 22, 2018, we announced that our board of directors authorized the repurchase of up to \$200 million of our Class A common stock. This repurchase program has no expiration but may be suspended or terminated by the board of directors at any time. Under the repurchase program, we are authorized to repurchase, from time to time, outstanding shares of Class A common stock in the open market, through privately negotiated transactions, or otherwise, including pursuant to a Rule 10b5-1 plan.

The actual timing, number and value of shares repurchased will be determined by the Company in its discretion and will depend on a number of factors, including market conditions, applicable legal requirements, our capital needs and whether there is a better alternative use of capital. We have no obligation to repurchase any amount of Class A common stock under the program.

Credit Agreement and Convertible Notes

For information regarding our credit agreement and convertible notes, see Note 11, Credit Agreement, and Note 12, Convertible Debt, respectively, included in Part I, Item 1, Unaudited Consolidated and Condensed Financial Statements, of this Quarterly Report on Form 10-Q.

Off-Balance Sheet Arrangements

We do not engage in any off-balance sheet activities. We do not have any off-balance sheet interest in variable interest entities, which include special purpose entities and other structured finance entities.

Contractual Obligations

There have been no material changes to our contractual obligations and estimates as compared to the contractual obligations described in Contractual Obligations included in Part II, Item 7, Management's Discussion and Analysis of Financial Condition and Results of Operations, of the Company's Annual Report on Form 10-K for the year ended December 31, 2017, except as disclosed in Note 6, Commitments and Contingencies, included in Part I, Item 1, Unaudited Consolidated and Condensed Financial Statements, of this Quarterly Report on Form 10-Q.

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Critical Accounting Policies

Our financial statements are prepared in accordance with accounting principles generally accepted in the U.S. The preparation of our financial statements and related disclosures requires us to make estimates, assumptions and judgments that affect the reported amount of assets, liabilities, net revenue, costs and expenses and related disclosures. We believe that the estimates, assumptions and judgments involved in the accounting policies described below have the greatest potential impact on our financial statements and, therefore, we consider these to be our critical accounting policies. Accordingly, we evaluate our estimates and assumptions on an ongoing basis. Our actual results may differ from these estimates under different assumptions and conditions.

There have been no material changes to our critical accounting policies and estimates as compared to the critical accounting policies and estimates described in Note 2, Summary of Significant Accounting Policies, included in Part II, Item 8, Financial Statements and Supplementary Data, of the Company's Annual Report on Form 10-K for the year ended December 31, 2017, except as disclosed in Note 2, Summary of Significant Accounting Policies - Revenue Recognition, included in Part I, Item 1, Unaudited Consolidated and Condensed Financial Statements, of this Quarterly Report on Form 10-Q.

Recent Accounting Pronouncements

For information about recent accounting pronouncements, see Note 14, Recent Accounting Pronouncements, included in Part I, Item 1, Unaudited Consolidated and Condensed Financial Statements, of this Quarterly Report on Form 10-Q.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We have operations both within the U.S. and internationally, and we are exposed to market risks in the ordinary course of our business, including the effects of foreign currency fluctuations, interest rate changes and inflation. Information relating to quantitative and qualitative disclosures about these market risks is set forth below.

Interest Rate Sensitivity

Cash and cash equivalents and short-term and long-term investments were held primarily in cash deposits, certificates of deposit, money market funds, and corporate debt. The fair value of our cash, cash equivalents and short-term and long-term investments would not be significantly affected by either an increase or decrease in interest rates due mainly to the short-term nature of these instruments.

Our convertible notes, which were issued in September 2017, carry a fixed interest rate of 0.375% per year. Since the convertible notes bear interest at a fixed rate, we have no direct financial statement risk associated with changes in interest rates.

Interest on the revolving line of credit incurred pursuant to the credit agreement described herein would accrue at a floating rate based on a formula tied to certain market rates at the time of incurrence; however, we do not expect that any change in prevailing interest rates will have a material impact on our results of operations.

Foreign Currency Risk

Most of our sales are denominated in U.S. dollars, and therefore, our revenue is not currently subject to significant foreign currency risk. Our operating expenses are denominated in the currencies of the countries in which our operations are located or in which net revenue is generated, and may be subject to fluctuations due to changes in foreign currency exchange rates, particularly changes in the British Pound, Euro and Canadian Dollar. Fluctuations in foreign currency exchange rates may cause us to recognize transaction gains and losses in our statement of operations, and our continued international expansion increases our exposure to exchange rate fluctuations that could impact our future results of operations. To date, foreign currency transaction gains and losses have not been material to our financial statements, and we have not engaged in any foreign currency hedging transactions.

Inflation

We do not believe that inflation has had a material effect on our business, financial condition or results of operations. We continue to monitor the impact of inflation in order to minimize its effects through pricing strategies, productivity improvements and cost reductions. If our costs were to become subject to significant inflationary pressures, we may not be able to fully offset such higher costs through price increases. Our inability or failure to do so could harm our business, financial condition and results of operations.

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ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q. The term "disclosure controls and procedures," as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended, or the Exchange Act, means controls and other procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the rules and forms of the Securities and Exchange Commission, or SEC. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, as appropriate to allow timely decisions regarding required disclosure. Management recognizes that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving their objectives and management necessarily applies its judgment in evaluating the cost-benefit relationship of possible controls and procedures. Based on the evaluation of our disclosure controls and procedures as of the end of the period covered by this Quarterly Report on Form 10-Q, our chief executive officer and chief financial officer concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

Changes in Internal Control Over Financial Reporting

There were no changes in our internal control over financial reporting identified in connection with the evaluation required by Rule 13a-15(d) or 15d-15(d) of the Exchange Act during the period covered by this Quarterly Report on Form 10-Q that materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II

OTHER INFORMATION

Item 1. Legal Proceedings

For information regarding our legal proceedings, see Note 6, Commitments and Contingencies - Legal Matters, included in Part I, Item 1, Unaudited Consolidated and Condensed Financial Statements, of this Quarterly Report on Form 10-Q, which is incorporated into this item by reference.

Item 1A. Risk Factors

There are no material changes from the risk factors previously disclosed in Part I, Item 1A, Risk Factors, of our Annual Report on Form 10-K for the year ended December 31, 2017.

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

Recent Sales of Unregistered Securities

During the three months ended September 30, 2018, we issued 96,956 shares of Class B common stock upon the vesting of outstanding restricted stock units, net of shares withheld to satisfy statutory minimum tax withholding obligations. The issuance of these securities was pursuant to written compensatory plans or arrangements with our employees, consultants, advisors and directors in reliance on the exemption provided by Rule 701 promulgated under the Securities Act, relative to transactions by an issuer not involving any public offering, to the extent an exemption from registration was required.

Recent Purchases of Equity Securities

During the three months ended September 30, 2018, we did not repurchase any shares of our common stock.

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| Item 6. Exhibits. | | Incorporated by Reference | | | |
|--|--|---------------------------|------|----------|---------|
| Exhibit | | Filed | File | Filing | Exhibit |
| Number | Description | Herewith | Form | No. Date | Number |
| 31.1 | <u>Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u> | X | | | |
| 31.2 | <u>Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934, as amended, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u> | X | | | |
| 32.1# | <u>Certification of Chief Executive Officer pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u> | X | | | |
| 32.2# | <u>Certification of Chief Financial Officer pursuant to 18 U.S.C. §1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u> | X | | | |
| 101.INS | XBRL Instance Document | X | | | |
| 101.SCH | XBRL Taxonomy Extension Schema Document | X | | | |
| 101.CAL | XBRL Taxonomy Calculation Linkbase Document | X | | | |
| 101.DEF | XBRL Taxonomy Definition Linkbase Document | X | | | |
| 101.LAB | XBRL Taxonomy Labels Linkbase Document | X | | | |
| 101.PRE | XBRL Taxonomy Presentation Linkbase Document | X | | | |
| + Indicates a management contract or compensatory plan | | | | | |

This certification is deemed not filed for purposes of section 18 of the Securities Exchange Act of 1934, as amended # (Exchange Act), or otherwise subject to the liability of that section, nor shall it be deemed incorporated by reference into any filing under the Securities Act of 1933, as amended or the Exchange Act.

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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.

WAYFAIR INC.

Date: November 1, 2018 By: /s/ NIRAJ SHAH

Niraj Shah
Chief Executive Officer and President
(Principal Executive Officer)

Date: November 1, 2018 By: /s/ MICHAEL FLEISHER

Michael Fleisher
Chief Financial Officer
(Principal Financial and Accounting Officer)