UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended December 30, 2022

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: 1-8703

WESTERN DIGITAL CORPORATION
(Exact Name of Registrant as Specified in Its Charter)

Delaware	**33-0956711**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*
5601 Great Oaks Parkway San Jose, California	**95119**
(Address of principal executive offices)	*(Zip Code)*

Registrant's telephone number, including area code: (408) 717-6000

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading symbol(s)	Name of each exchange on which registered
Common Stock, $0.01 Par Value Per Share	WDC	The Nasdaq Stock Market LLC (Nasdaq Global Select Market)

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, a 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. ☐

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

As of the close of business on January 25, 2023, 319,322,335 shares of common stock, par value $0.01 per share, were outstanding.

WESTERN DIGITAL CORPORATION

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PART I. FINANCIAL INFORMATION

PART II. OTHER INFORMATION

Unless otherwise indicated, references herein to specific years and quarters are to our fiscal years and fiscal quarters, and references to financial information are on a consolidated basis. As used herein, the terms “we,” “us,” “our,” the “Company,” “WDC” and “Western Digital” refer to Western Digital Corporation and its subsidiaries, unless we state, or the context indicates, otherwise.

WDC, a Delaware corporation, is the parent company of our data storage business. Our principal executive offices are located at 5601 Great Oaks Parkway, San Jose, California 95119. Our telephone number is (408) 717-6000.

Western Digital, the Western Digital logo, SanDisk, and WD are registered trademarks or trademarks of Western Digital or its affiliates in the U.S. and/or other countries. All other trademarks, registered trademarks and/or service marks, indicated or otherwise, are the property of their respective owners.

FORWARD-LOOKING STATEMENTS

This document contains forward-looking statements within the meaning of the federal securities laws. Any statements that do not relate to historical or current facts or matters are forward-looking statements. You can identify some of the forward-looking statements by the use of forward-looking words, such as "may," "will," "could," "would," "project," "believe," "anticipate," "expect," "estimate," "continue," "potential," "plan," "forecast," and the like, or the use of future tense. Statements concerning current conditions may also be forward-looking if they imply a continuation of current conditions. Examples of forward-looking statements include, but are not limited to, statements concerning: expectations regarding the global macroeconomic environment; the effects of the COVID-19 pandemic; expectations regarding supply chain conditions and constraints; expectations regarding demand trends and market conditions for our products and expected future financial performance; expectations regarding our product momentum and product development and technology plans; expectations regarding capital expenditure plans and investments, including relating to our Flash Ventures joint venture with Kioxia Corporation ("Kioxia"), and sources of funding for those expenditures; expectations regarding our effective tax rate and our unrecognized tax benefits; and our beliefs regarding the sufficiency of our available liquidity to meet our working capital, debt and capital expenditure needs.

These forward-looking statements are based on management's current expectations, represent the most current information available to the Company as of the date of this Quarterly Report on Form 10-Q and are subject to a number of risks, uncertainties and other factors that could cause actual results or performance to differ materially from those expressed in the forward-looking statements. These risks and uncertainties include, but are not limited to:

- *volatility in global economic conditions;*
- *future responses to and effects of the COVID-19 pandemic or other similar global health crises;*
- *impact of business and market conditions;*
- *the outcome and impact of our ongoing strategic review, including with respect to customer and supplier relationships, regulatory and contractual restrictions, stock price volatility and the diversion of management's attention from ongoing business operations and opportunities;*
- *impact of competitive products and pricing;*
- *our development and introduction of products based on new technologies and expansion into new data storage markets;*
- *risks associated with cost saving initiatives, restructurings, acquisitions, divestitures, mergers, joint ventures and our strategic relationships;*
- *difficulties or delays in manufacturing or other supply chain disruptions;*
- *hiring and retention of key employees;*
- *our level of debt and other financial obligations;*
- *changes to our relationships with key customers;*
- *disruptions in operations from cybersecurity incidents or other system security risks;*
- *actions by competitors;*
- *risks associated with compliance with changing legal and regulatory requirements and the outcome of legal proceedings; and*
- *the other risks and uncertainties disclosed in Part I, Item 1A of our Annual Report on Form 10-K for the year ended July 1, 2022 (the "2022 Annual Report on Form 10-K").*

You are urged to carefully review the disclosures we make concerning these risks and review the additional disclosures we make concerning material risks and other factors that may affect the outcome of our forward-looking statements and our business and operating results, including those made in Part I, Item 1A of our 2022 Annual Report on Form 10-K and any of those made in our other reports filed with the Securities and Exchange Commission, including under "Risk Factors" in Item 1A of subsequent Annual Reports on Form 10-K and Quarterly Reports on Form 10-Q that may from time to time amend, supplement or supersede the risks and uncertainties disclosed in the 2022 Annual Report on Form 10-K. You are cautioned not to place undue reliance on the forward-looking statements included in this Quarterly Report on Form 10-Q, which speak only as of the date of this document. We do not intend, and undertake no obligation, to update or revise these forward-looking statements to reflect new information or events after the date of this document or to reflect the occurrence of unanticipated events, except as required by law.

PART I. FINANCIAL INFORMATION

Item 1. *Financial Statements (unaudited)*

WESTERN DIGITAL CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEETS
(in millions, except par value)
(Unaudited)

	December 30, 2022	July 1, 2022
ASSETS		
Current assets:		
Cash and cash equivalents	$ 1,871	$ 2,327
Accounts receivable, net	1,905	2,804
Inventories	3,773	3,638
Other current assets	832	684
Total current assets	8,381	9,453
Property, plant and equipment, net	3,688	3,670
Notes receivable and investments in Flash Ventures	1,357	1,396
Goodwill	10,041	10,041
Other intangible assets, net	135	213
Other non-current assets	1,445	1,486
Total assets	$ 25,047	$ 26,259
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$ 1,193	$ 1,902
Accounts payable to related parties	368	320
Accrued expenses	1,410	1,636
Income taxes payable	1,025	869
Accrued compensation	348	510
Current portion of long-term debt	38	—
Total current liabilities	4,382	5,237
Long-term debt	7,033	7,022
Other liabilities	1,517	1,779
Total liabilities	12,932	14,038
Commitments and contingencies (Notes 10, 11, 13 and 16)		
Shareholders' equity:		
Common stock, $0.01 par value; authorized — 450 shares; issued — 319 shares and 315 shares, respectively; outstanding — 319 shares and 315 shares, respectively	3	3
Additional paid-in capital	3,770	3,733
Accumulated other comprehensive loss	(369)	(554)
Retained earnings	8,711	9,039
Total shareholders' equity	12,115	12,221
Total liabilities and shareholders' equity	$ 25,047	$ 26,259

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

WESTERN DIGITAL CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(in millions, except per share amounts)
(Unaudited)

	Three Months Ended		Six Months Ended	
	December 30, 2022	December 31, 2021	December 30, 2022	December 31, 2021
Revenue, net	$ 3,107	$ 4,833	$ 6,843	$ 9,884
Cost of revenue	2,579	3,250	5,334	6,636
Gross profit	528	1,583	1,509	3,248
Operating expenses:				
Research and development	523	575	1,075	1,153
Selling, general and administrative	250	279	497	570
Employee termination, asset impairment, and other charges	76	2	100	20
Total operating expenses	849	856	1,672	1,743
Operating income (loss)	(321)	727	(163)	1,505
Interest and other income (expense):				
Interest income	3	1	5	3
Interest expense	(73)	(76)	(143)	(154)
Other income (expense), net	6	(6)	—	(4)
Total interest and other expense, net	(64)	(81)	(138)	(155)
Income (loss) before taxes	(385)	646	(301)	1,350
Income tax expense	61	82	118	176
Net income (loss)	$ (446)	$ 564	$ (419)	$ 1,174
Income (loss) per common share:				
Basic	$ (1.40)	$ 1.81	$ (1.32)	$ 3.77
Diluted	$ (1.40)	$ 1.79	$ (1.32)	$ 3.73
Weighted average shares outstanding:				
Basic	318	312	317	311
Diluted	318	315	317	315

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

WESTERN DIGITAL CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(in millions)
(Unaudited)

	Three Months Ended		Six Months Ended	
	December 30, 2022	December 31, 2021	December 30, 2022	December 31, 2021
Net income (loss)	$ (446)	$ 564	$ (419)	$ 1,174
Other comprehensive income (loss), before tax:				
Actuarial pension gain	—	—	—	1
Foreign currency translation adjustment	95	(45)	15	(41)
Net unrealized gain (loss) on derivative contracts and available-for-sale securities	288	(10)	212	23
Total other comprehensive income (loss), before tax	383	(55)	227	(17)
Income tax benefit (expense) related to items of other comprehensive income (loss), before tax	(58)	5	(42)	(3)
Other comprehensive income (loss), net of tax	325	(50)	185	(20)
Total comprehensive income (loss)	$ (121)	$ 514	$ (234)	$ 1,154

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

WESTERN DIGITAL CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(in millions)
(Unaudited)

	Six Months Ended	
	December 30, 2022	December 31, 2021
Cash flows from operating activities		
Net income (loss)	$ (419)	$ 1,174
Adjustments to reconcile net income to net cash provided by operations:		
Depreciation and amortization	430	492
Stock-based compensation	172	163
Deferred income taxes	25	38
Loss on disposal of assets	1	1
Non-cash portion of asset impairment	15	—
Amortization of debt issuance costs and discounts	5	21
Other non-cash operating activities, net	69	13
Changes in:		
Accounts receivable, net	899	(486)
Inventories	(135)	(30)
Accounts payable	(521)	96
Accounts payable to related parties	49	(9)
Accrued expenses	(226)	81
Income taxes payable	156	(34)
Accrued compensation	(162)	(66)
Other assets and liabilities, net	(317)	(267)
Net cash provided by operating activities	41	1,187
Cash flows from investing activities		
Purchases of property, plant and equipment	(578)	(551)
Proceeds from the sale of property, plant and equipment	—	12
Proceeds from dispositions of business	7	—
Notes receivable issuances to Flash Ventures	(235)	(337)
Notes receivable proceeds from Flash Ventures	317	320
Strategic investments and other, net	7	(13)
Net cash used in investing activities	(482)	(569)
Cash flows from financing activities		
Issuance of stock under employee stock plans	48	60
Taxes paid on vested stock awards under employee stock plans	(55)	(80)
Repayment of debt	—	(2,425)
Proceeds from debt	—	998
Repayments of revolving credit facility	(1,180)	—
Proceeds from revolving credit facility	1,180	—
Debt issuance costs	(5)	(9)
Net cash used in financing activities	(12)	(1,456)
Effect of exchange rate changes on cash	(3)	(1)
Net decrease in cash and cash equivalents	(456)	(839)
Cash and cash equivalents, beginning of year	2,327	3,370
Cash and cash equivalents, end of period	$ 1,871	$ 2,531
Supplemental disclosure of cash flow information:		
Cash paid for income taxes	$ 192	$ 312
Cash paid for interest	$ 138	$ 129

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

WESTERN DIGITAL CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(in millions)
(Unaudited)

	Common Stock		Treasury Stock		Additional Paid-In Capital	Accumulated Other Comprehensive Loss	Retained Earnings	Total Shareholders' Equity
	Shares	Amount	Shares	Amount				
Balance at July 1, 2022	315	$ 3	—	$ —	$ 3,733	$ (554)	$ 9,039	$ 12,221
Net income	—	—	—	—	—	—	27	27
Adoption of new accounting standards	—	—	—	—	(128)	—	91	(37)
Employee stock plans	3	—	—	—	(50)	—	—	(50)
Stock-based compensation	—	—	—	—	86	—	—	86
Foreign currency translation adjustment	—	—	—	—	—	(80)	—	(80)
Net unrealized loss on derivative contracts	—	—	—	—	—	(60)	—	(60)
Balance at September 30, 2022	318	3	—	—	3,641	(694)	9,157	12,107
Net loss	—	—	—	—	—	—	(446)	(446)
Employee stock plans	1	—	—	—	43	—	—	43
Stock-based compensation	—	—	—	—	86	—	—	86
Foreign currency translation adjustment	—	—	—	—	—	97	—	97
Net unrealized gain on derivative contracts	—	—	—	—	—	228	—	228
Balance at December 30, 2022	319	$ 3	—	$ —	$ 3,770	$ (369)	$ 8,711	$ 12,115

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

WESTERN DIGITAL CORPORATION
CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY
(in millions)
(Unaudited)

	Common Stock		Treasury Stock					
	Shares	Amount	Shares	Amount	Additional Paid-In Capital	Accumulated Other Comprehensive Loss	Retained Earnings	Total Shareholders' Equity
Balance at July 2, 2021	312	$ 3	(4)	$ (232)	$ 3,608	$ (197)	$ 7,539	$ 10,721
Net income	—	—	—	—	—	—	610	610
Employee stock plans	—	—	3	207	(283)	—	—	(76)
Stock-based compensation	—	—	—	—	76	—	—	76
Actuarial pension gain	—	—	—	—	—	1	—	1
Foreign currency translation adjustment	—	—	—	—	—	4	—	4
Net unrealized gain on derivative contracts	—	—	—	—	—	25	—	25
Balance at October 1, 2021	312	3	(1)	(25)	3,401	(167)	8,149	11,361
Net income	—	—	—	—	—	—	564	564
Employee stock plans	1	—	1	25	31	—	—	56
Stock-based compensation	—	—	—	—	87	—	—	87
Foreign currency translation adjustment	—	—	—	—	—	(45)	—	(45)
Net unrealized loss on derivative contracts	—	—	—	—	—	(5)	—	(5)
Balance at December 31, 2021	313	$ 3	—	$ —	$ 3,519	$ (217)	$ 8,713	$ 12,018

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

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1. Organization and Basis of Presentation

Western Digital Corporation ("Western Digital" or the "Company") is a leading developer, manufacturer, and provider of data storage devices and solutions based on both flash-based products ("Flash") and hard disk drives ("HDD") technologies. With dedicated Flash and HDD business units driving advancements in memory technologies, the Company creates and drives innovations needed to help customers capture, preserve, access, and transform an ever-increasing diversity of data.

The accounting policies followed by the Company are set forth in Part II, Item 8, Note 1, *Organization and Basis of Presentation,* of the Notes to Consolidated Financial Statements included in the Company's Annual Report on Form 10-K for the year ended July 1, 2022. In the opinion of management, all adjustments necessary to fairly state the Condensed Consolidated Financial Statements have been made. All such adjustments are of a normal, recurring nature. Certain information and footnote disclosures normally included in the Consolidated Financial Statements prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP") have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). These Condensed Consolidated Financial Statements should be read in conjunction with the Consolidated Financial Statements and the notes thereto included in the Company's Annual Report on Form 10-K for the year ended July 1, 2022. The results of operations for interim periods are not necessarily indicative of results to be expected for the full year.

Fiscal Year

The Company's fiscal year ends on the Friday nearest to June 30 and typically consists of 52 weeks. Approximately every five to six years, the Company reports a 53-week fiscal year to align the fiscal year with the foregoing policy. Fiscal years 2023, which ends on June 30, 2023, and 2022, which ended on July 1, 2022, are each comprised of 52 weeks, with all quarters presented consisting of 13 weeks.

Segment Reporting

The Company manufactures, markets, and sells data storage devices and solutions in the U.S. and in foreign countries through its sales personnel, dealers, distributors, retailers, and subsidiaries. The Company manages and reports under two reportable segments: Flash and HDD.

The Company's Chief Operating Decision Maker ("CODM") evaluates performance of the Company and makes decisions regarding allocation of resources based on each operating segment's net revenue and gross margin. Because of the integrated nature of the Company's production and distribution activities, separate segment asset measures are not available or reviewed by the CODM to evaluate the performance of or to allocate resources to the segments.

Use of Estimates

Company management has made estimates and assumptions relating to the reporting of certain assets and liabilities in conformity with U.S. GAAP. These estimates and assumptions have been applied using methodologies that are consistent throughout the periods presented with consideration given to the potential impacts of current macroeconomic conditions. However, actual results could differ materially from these estimates.

Note 2. Recent Accounting Pronouncements

Accounting Pronouncements Recently Adopted

In August 2020, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2020-06, "Debt—Debt with Conversion and Other Options (Subtopic 470-20) and Derivatives and Hedging—Contracts in Entity's Own Equity (Subtopic 815-40): Accounting for Convertible Instruments and Contracts in an Entity's Own Equity" ("ASU 2020-06"). ASU 2020-06 reduces the number of accounting models for convertible debt instruments and convertible preferred stock and results in fewer instruments with embedded conversion features being separately recognized from the host contract as compared with prior standards. Those instruments that do not have a separately recognized embedded conversion feature will no longer recognize a debt issuance discount related to such a conversion feature and would recognize less interest expense on a periodic basis. Additionally, the ASU amends the calculation of the share dilution impact related to a conversion feature and eliminates the treasury method as an option. The Company adopted the new standard effective July 2, 2022, the first day of the year ending June 30, 2023, using the modified retrospective method. On the date of adoption, the Company recorded a reduction in Additional Paid-In Capital of $128 million, a reduction of unamortized debt discount of $48 million, a reduction of deferred income tax liabilities of $11 million, and an increase to retained earnings of $91 million for the after-tax impact of previously recognized amortization of the debt discount associated with the Company's convertible senior notes.

In November 2021, the FASB issued ASU No. 2021-10, "Government Assistance (Topic 832): Disclosures by Business Entities about Government Assistance" ("ASU 2021-10"). ASU 2021-10 increases the transparency of government assistance received by requiring most business entities to disclose information about government assistance received, including (1) the types of assistance, (2) the entity's accounting for the assistance, and (3) the effect of the assistance on an entity's financial statements. This ASU is effective for fiscal years (and interim periods within those fiscal years) beginning after December 15, 2021, which for the Company is the first quarter of 2023. The Company adopted this ASU on July 2, 2022, the first day of the year ending June 30, 2023, and the adoption did not have a material impact on its Condensed Consolidated Financial Statements.

Recently Issued Accounting Pronouncements Not Yet Adopted

In September 2022, the FASB issued ASU No. 2022-04, "Liabilities-Supplier Finance Programs (Subtopic 405-50): Disclosure of Supplier Finance Program Obligations". This guidance requires annual and interim disclosures for entities that use supplier finance programs in connection with the purchase of goods and services. The ASU is effective for fiscal years beginning after December 15, 2022, with early adoption permitted, except for the amendment on rollforward information, which is effective for fiscal years beginning after December 15, 2023. The Company is currently evaluating the extent of the impact of this ASU on its Condensed Consolidated Financial Statements.

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 3. Business Segments, Geographic Information, and Concentrations of Risk

The following table summarizes the operating performance of the Company's reportable segments:

	Three Months Ended		Six Months Ended	
	December 30, 2022	December 31, 2021	December 30, 2022	December 31, 2021
	$ in millions			
Net revenue:				
Flash	$ 1,657	$ 2,620	$ 3,379	$ 5,110
HDD	1,450	2,213	3,464	4,774
Total net revenue	$ 3,107	$ 4,833	$ 6,843	$ 9,884
Gross profit:				
Flash	$ 240	$ 946	$ 662	$ 1,867
HDD	300	677	874	1,469
Total gross profit for segments	540	1,623	1,536	3,336
Unallocated corporate items:				
Stock-based compensation expense	(12)	(14)	(26)	(23)
Amortization of acquired intangible assets	—	(26)	(1)	(65)
Total unallocated corporate items	(12)	(40)	(27)	(88)
Consolidated gross profit	$ 528	$ 1,583	$ 1,509	$ 3,248
Gross margin:				
Flash	14.5 %	36.1 %	19.6 %	36.5 %
HDD	20.7 %	30.6 %	25.2 %	30.8 %
Consolidated gross margin	17.0 %	32.8 %	22.1 %	32.9 %

Disaggregated Revenue

The Company's broad portfolio of technology and products address multiple end markets. Cloud represents a large and growing end market comprised primarily of products for public or private cloud environments and end customers, which the Company believes it is uniquely positioned to address as the only provider of both Flash and HDD. Through the Client end market, the Company provides its original equipment manufacturer ("OEM") and channel customers a broad array of high-performance flash and hard drive solutions across personal computer, mobile, gaming, automotive, virtual reality headsets, at-home entertainment, and industrial spaces. The Consumer end market is highlighted by the Company's broad range of retail and other end-user products, which capitalize on the strength of the Company's product brand recognition and vast points of presence around the world.

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

The Company’s disaggregated revenue information is as follows:

	Three Months Ended		Six Months Ended	
	December 30, 2022	December 31, 2021	December 30, 2022	December 31, 2021
	(in millions)			
Revenue by End Market				
Cloud	$ 1,224	$ 1,920	$ 3,053	$ 4,145
Client	1,089	1,854	2,318	3,707
Consumer	794	1,059	1,472	2,032
Total Revenue	$ 3,107	$ 4,833	$ 6,843	$ 9,884
Revenue by Geography				
Asia	$ 1,494	$ 2,610	$ 3,180	$ 5,285
Americas	1,090	1,407	2,513	3,021
Europe, Middle East and Africa	523	816	1,150	1,578
Total Revenue	$ 3,107	$ 4,833	$ 6,843	$ 9,884

The Company’s top 10 customers accounted for 47% and 48% of its net revenue for the three and six months ended December 30, 2022, respectively, and 46% and 44% of its net revenue for the three and six months ended December 31, 2021, respectively. For the three and six months ended December 30, 2022 and December 31, 2021, no single customer accounted for 10% or more of the Company’s net revenue.

Goodwill

The following table provides a summary of goodwill activity for the period:

	Flash	HDD	Total
		(in millions)	
Balance at July 1, 2022	$ 5,718	$ 4,323	$ 10,041
Foreign currency translation adjustment	—	—	—
Balance at December 30, 2022	$ 5,718	$ 4,323	$ 10,041

Goodwill is not amortized. Instead, it is tested for impairment annually as of the beginning of the Company’s fourth quarter, or more frequently if events or changes in circumstances indicate that goodwill may be impaired. The Company uses qualitative factors to determine whether goodwill is more-likely-than-not impaired and whether a quantitative test for impairment is considered necessary. If the Company concludes from the qualitative assessment that goodwill is more likely than not impaired, the Company is required to perform a quantitative approach to determine the amount of impairment.

As of December 30, 2022, management identified several continuing factors, including changes in macroeconomic conditions and recent declines of the Company’s market stock price, that warranted quantitative analyses of impairments for both the Flash and HDD reporting units as of such date. The fair value of each operating segment was based on a weighting of two valuation methodologies: an income approach and a market approach.

The income approach was based on the present value of the projected discounted cash flows (“DCF”) expected to be generated by the operating segment. Those projections required the use of significant estimates and assumptions specific to the reporting unit as well as those based on general economic conditions, which included, among other factors, revenue growth rates, gross margins, operating costs, capital expenditures, assumed tax rates and other assumptions deemed reasonable by management. The present value was based on applying a weighted average cost of capital (“WACC”) which considered long-term interest rates and cost of equity based on the Company’s risk profile.

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

The market approach was based on a guideline company method, which analyzed market multiples of revenue and earnings before interest, taxes, depreciation and amortization ("EBITDA") for a group of comparable public companies.

The Company reconciled the aggregated estimated fair value of both operating segments to the Company's market capitalization, including consideration of a control premium representing the estimated amount a market participant would pay to obtain a controlling interest in the Company.

As of December 30, 2022, the fair value derived from those valuation methodologies exceeded the carrying value by 9% and 28% for Flash and HDD, respectively. There were no impairment charges recorded for the three and six months ended December 30, 2022.

The Company is required to use judgment when applying the goodwill impairment test, including the assignment of assets and liabilities to reporting units, and determination of the fair value of each reporting unit. In addition, the estimates used to determine the fair value of reporting units as well as their actual carrying value may change based on future changes in the Company's results of operations, macroeconomic conditions or other factors. Changes in these estimates could materially affect the Company's assessment of the fair value and goodwill impairment. In addition, if negative macroeconomic conditions continue or worsen or the Company's stock price decreases further for a sustained period of time, goodwill could become impaired, which could result in an impairment charge and materially adversely affect the Company's financial condition results of operations.

Note 4. Revenues

Contract assets represent the Company’s rights to consideration where performance obligations are completed but the customer payments are not due until another performance obligation is satisfied. The Company did not have any contract assets as of either December 30, 2022 or July 1, 2022. Contract liabilities relate to customers’ payments in advance of performance under the contract and primarily relate to remaining performance obligations under professional service and support and maintenance contracts. Contract liabilities as of December 30, 2022 and July 1, 2022 and changes in contract liabilities for the six months ended December 30, 2022 and December 31, 2021 were not material.

The Company incurs sales commissions and other direct incremental costs to obtain sales contracts. The Company has applied the practical expedient to recognize the direct incremental costs of obtaining contracts as an expense when incurred if the amortization period is expected to be one year or less or the amount is not material, with these costs charged to Selling, general and administrative expenses. The Company had no direct incremental costs to obtain contracts that have an expected benefit of greater than one year.

The Company applies the practical expedients and does not disclose transaction price allocated to the remaining performance obligations for (i) arrangements that have an original expected duration of one year or less, which mainly consist of the support and maintenance contracts, and (ii) variable consideration amounts for sale-based or usage-based royalties for intellectual property (“IP”) license arrangements, which typically have a duration of longer than one year. Remaining performance obligations are mainly attributed to right-to-access patent license arrangements, professional service arrangements and customer support and service contracts which will be recognized over the remaining contract period. The transaction price allocated to the remaining performance obligations as of December 30, 2022 was $17 million, which is mainly attributable to the functional IP license and professional service arrangements. The Company expects to recognize this amount as revenue as follows: $14 million during the remainder of 2023, and $3 million in 2024 and thereafter.

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Note 5. Supplemental Financial Statement Data

Accounts receivable, net

From time to time, in connection with factoring agreements, the Company sells trade accounts receivable without recourse to third party purchasers in exchange for cash. During the six months ended December 30, 2022, the Company sold trade accounts receivable aggregating $391 million. The Company did not sell any trade accounts receivable during the six months ended December 31, 2021. The discounts on the trade accounts receivable sold were not material and were recorded within Other income (expense), net in the Condensed Consolidated Statements of Operations. As of December 30, 2022 and July 1, 2022, the amount of factored receivables that remained outstanding was $100 million and $300 million, respectively.

Inventories

	December 30, 2022	July 1, 2022
	(in millions)	
Inventories:		
Raw materials and component parts	$ 1,968	$ 1,603
Work-in-process	966	1,162
Finished goods	839	873
Total inventories	$ 3,773	$ 3,638

Property, plant and equipment, net

	December 30, 2022	July 1, 2022
	(in millions)	
Property, plant and equipment:		
Land	$ 269	$ 269
Buildings and improvements	1,953	1,920
Machinery and equipment	8,692	8,642
Computer equipment and software	506	494
Furniture and fixtures	54	54
Construction-in-process	690	591
Property, plant and equipment, gross	12,164	11,970
Accumulated depreciation	(8,476)	(8,300)
Property, plant and equipment, net	$ 3,688	$ 3,670

Other Intangible assets, net

	December 30, 2022	July 1, 2022
	(in millions)	
Other Intangible assets:		
Finite-lived intangible assets	$ 5,492	$ 5,493
In-process research and development	80	80
Accumulated amortization	(5,437)	(5,360)
Other Intangible assets, net	$ 135	$ 213

As part of prior acquisitions, the Company recorded at the time of the acquisition acquired in-process research and development ("IPR&D") for projects in progress that had not yet reached technological feasibility. IPR&D is initially accounted for as an indefinite-lived intangible asset. Once a project reaches technological feasibility, the Company reclassifies the balance to existing technology and begins to amortize the intangible asset over its estimated useful life.

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Product warranty liability

Changes in the warranty accrual were as follows:

	Three Months Ended		Six Months Ended	
	December 30, 2022	December 31, 2021	December 30, 2022	December 31, 2021
	(in millions)			
Warranty accrual, beginning of period	$ 340	$ 370	$ 345	$ 363
Charges to operations	25	36	57	76
Utilization	(60)	(28)	(94)	(51)
Changes in estimate related to pre-existing warranties	(16)	(27)	(19)	(37)
Warranty accrual, end of period	$ 289	$ 351	$ 289	$ 351

The current portion of the warranty accrual is classified in Accrued expenses and the long-term portion is classified in Other liabilities as noted below:

	December 30, 2022	July 1, 2022
	(in millions)	
Warranty accrual:		
Current portion (included in Accrued expenses)	$ 131	$ 162
Long-term portion (included in Other liabilities)	158	183
Total warranty accrual	$ 289	$ 345

Other liabilities

	December 30, 2022	July 1, 2022
	(in millions)	
Other liabilities:		
Non-current net tax payable	$ 458	$ 659
Non-current portion of unrecognized tax benefits	452	477
Other non-current liabilities	607	643
Total other liabilities	$ 1,517	$ 1,779

Accumulated other comprehensive loss

Accumulated other comprehensive loss (“AOCI”), net of tax refers to expenses, gains and losses that are recorded as an element of shareholders’ equity but are excluded from net income. The following table illustrates the changes in the balances of each component of AOCI:

	Actuarial Pension Losses	Foreign Currency Translation Adjustment	Unrealized Losses on Derivative Contracts	Total Accumulated Comprehensive Loss
	(in millions)			
Balance at July 1, 2022	$ (11)	$ (277)	$ (266)	$ (554)
Other comprehensive income before reclassifications	—	15	35	50
Amounts reclassified from accumulated other comprehensive loss	—	—	177	177
Income tax benefit related to items of other comprehensive loss	—	2	(44)	(42)
Net current-period other comprehensive income	—	17	168	185
Balance at December 30, 2022	$ (11)	$ (260)	$ (98)	$ (369)

During the three and six months ended December 30, 2022, the amounts reclassified out of AOCI were losses related to foreign exchange contracts and gains related to interest rate swap contracts. Losses reclassified out of AOCI related to foreign exchange contracts were $119 million and $181 million for the three and six months ended December 30, 2022, respectively, that were substantially charged to Cost of revenue in the Condensed Consolidated Statements of Operations. Gains reclassified out of AOCI related to interest rate swap contracts were $6 million and $4 million for the three and six months ended December 30, 2022, respectively, that were charged to Interest expense in the Condensed Consolidated Statements of Operations.

As of December 30, 2022, substantially all existing net losses related to cash flow hedges recorded in AOCI are expected to be reclassified to earnings within the next twelve months. In addition, as of December 30, 2022, the Company did not have any foreign exchange forward contracts with credit-risk-related contingent features.

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Note 6. Fair Value Measurements and Investments

Financial Instruments Carried at Fair Value

Financial assets and liabilities that are remeasured and reported at fair value at each reporting period are classified and disclosed in one of the following three levels:

Level 1. Quoted prices in active markets for identical assets or liabilities.

Level 2. Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3. Inputs that are unobservable for the asset or liability and that are significant to the fair value of the assets or liabilities.

The following tables present information about the Company's financial assets and liabilities that are measured at fair value on a recurring basis as of December 30, 2022 and July 1, 2022, and indicate the fair value hierarchy of the valuation techniques utilized to determine such values:

	December 30, 2022			
	Level 1	Level 2	Level 3	Total
	(in millions)			
Assets:				
Cash equivalents - Money market funds	$ 435	$ —	$ —	$ 435
Foreign exchange contracts	—	105	—	105
Interest rate swap contracts	—	6	—	6
Total assets at fair value	$ 435	$ 111	$ —	$ 546
Liabilities:				
Foreign exchange contracts	$ —	$ 97	$ —	$ 97
Total liabilities at fair value	$ —	$ 97	$ —	$ 97

	July 1, 2022			
	Level 1	Level 2	Level 3	Total
	(in millions)			
Assets:				
Cash equivalents - Money market funds	$ 266	$ —	$ —	$ 266
Foreign exchange contracts	—	61	—	61
Interest rate swap contracts	—	3	—	3
Total assets at fair value	$ 266	$ 64	$ —	$ 330
Liabilities:				
Foreign exchange contracts	$ —	$ 316	$ —	$ 316
Total liabilities at fair value	$ —	$ 316	$ —	$ 316

During the periods presented, the Company had no transfers of financial assets and liabilities between levels and there were no changes in valuation techniques or the inputs used in the fair value measurement.

Financial Instruments Not Carried at Fair Value

For financial instruments where the carrying value (which includes principal adjusted for any unamortized issuance costs, and discounts or premiums) differs from fair value (which is based on quoted market prices), the following table represents the related carrying value and fair value for each of the Company's outstanding financial instruments. Each of the financial instruments presented below was categorized as Level 2 for all periods presented, based on the frequency of trading immediately prior to the end of the second quarter of 2023 and the fourth quarter of 2022, respectively.

	December 30, 2022		July 1, 2022	
	Carrying Value	Fair Value	Carrying Value	Fair Value
	(in millions)			
1.50% convertible notes due 2024	$ 1,097	$ 1,052	$ 1,048	$ 1,040
4.75% senior unsecured notes due 2026	2,292	2,169	2,291	2,205
Variable interest rate Term Loan A-2 maturing 2027	2,691	2,661	2,693	2,621
2.85% senior unsecured notes due 2029	496	388	495	412
3.10% senior unsecured notes due 2032	495	361	495	389
Total	$ 7,071	$ 6,631	$ 7,022	$ 6,667

Note 7. Derivative Instruments and Hedging Activities

As of December 30, 2022, the Company had outstanding foreign exchange forward contracts that were designated as either cash flow hedges or non-designated hedges. Substantially all of the contract maturity dates of these foreign exchange forward contracts do not exceed 12 months. In addition, the Company had outstanding pay-fixed interest rate swaps that were designated as cash flow hedges of variable rate interest payments through February 2023, on a portion of its term loans.

Changes in fair values of the non-designated foreign exchange contracts are recognized in Other income (expense), net and are largely offset by corresponding changes in the fair values of the foreign currency denominated monetary assets and liabilities. For each of the three and six months ended December 30, 2022 and December 31, 2021, total net realized and unrealized transaction and foreign exchange contract currency gains and losses were not material to the Company's Condensed Consolidated Financial Statements.

Unrealized gains or losses on designated cash flow hedges are recognized in AOCI. For more information regarding cash flow hedges, see Note 5, *Supplemental Financial Statement Data - Accumulated other comprehensive loss.*

Netting Arrangements

Under certain provisions and conditions within agreements with counterparties to the Company's foreign exchange forward contracts, subject to applicable requirements, the Company has the right of offset associated with the Company's foreign exchange forward contracts and is allowed to net settle transactions of the same currency with a single net amount payable by one party to the other. As of December 30, 2022 and July 1, 2022, the effect of rights of offset was not material and the Company did not offset or net the fair value amounts of derivative instruments in its Condensed Consolidated Balance Sheets.

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Note 8. Debt

Debt consisted of the following:

	December 30, 2022	July 1, 2022
	(in millions)	
1.50% convertible notes due 2024	$ 1,100	$ 1,100
4.75% senior unsecured notes due 2026	2,300	2,300
Variable interest rate Term Loan A-2 maturing 2027	2,700	2,700
2.85% senior unsecured notes due 2029	500	500
3.10% senior unsecured notes due 2032	500	500
Total debt	7,100	7,100
Issuance costs and debt discounts	(29)	(78)
Subtotal	7,071	7,022
Less current portion of long-term debt	(38)	—
Long-term debt	$ 7,033	$ 7,022

During the six months ended December 30, 2022, the Company drew and repaid $1.18 billion principal amount under its $2.25 billion revolving credit facility maturing in January 2027 (the “2027 Revolving Credit Facility”).

In December 2022, the Company amended the credit agreement governing the 2027 Revolving Credit Facility and Term Loan A-2 for the purposes of providing flexibility by adjusting the leverage ratio requirements of the financial covenant thereunder through the Company’s quarter ending September 27, 2024 (such period, the “Covenant Relief Period”). As amended, the Company is required to maintain a maximum ratio (“Leverage Ratio”) of total funded debt to trailing twelve-month Consolidated Adjusted EBITDA (as defined in the Credit Agreement) at the end of each quarter as follows:

Quarter ending:	Leverage ratio
December 30, 2022	3.25 to 1.00
March 31, 2023	3.75 to 1.00
June 30, 2023	4.75 to 1.00
September 29, 2023	5.00 to 1.00
December 29, 2023	4.75 to 1.00
March 29, 2024	4.50 to 1.00
June 28, 2024	4.25 to 1.00
September 27, 2024	3.75 to 1.00
December 27, 2024 and thereafter	3.25 to 1.00

As of December 30, 2022, the Company was in compliance with this financial covenant. The amendment also provides that the due date for amounts outstanding under the Credit Agreement will be accelerated from January 7, 2027 to November 2, 2023 if, as of that date, the Company does not have Cash and cash equivalents plus available unused capacity under its credit facilities that exceed by $1 billion the sum of the outstanding balance of the 1.50% convertible notes due 2024 plus the outstanding principal amount of any other debt maturing within 12 months. In addition, during the Covenant Relief Period, the amendment requires certain subsidiaries of the Company to provide guarantees if the corporate family ratings of the Company from at least two of Standard & Poor’s Ratings Services, Moody’s Investors Service, Inc. and Fitch, Inc. (the “Credit Rating Agencies”) drops below investment grade and includes limits on secured indebtedness and certain types of unsecured subsidiary indebtedness.

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In January 2023, the Company entered into a loan agreement (the “Delayed Draw Term Loan Agreement”), which allows the Company to draw a single unsecured loan of up to $875 million (the “Delayed Draw Term Loan”) through June 30, 2023. The Delayed Draw Term Loan Agreement may be terminated, at the election of the Company, at any time without premium or penalty, subject to certain conditions.

Any amount drawn under the Delayed Draw Term Loan Agreement will mature 364 days following the date of the initial draw. However, the due date will be accelerated to November 2, 2023 if conditions for acceleration of amounts due under the Credit Agreement have been triggered as described above.

The Delayed Draw Term Loan will bear interest, at the Company’s option, at a per annum rate equal to either (x) the Adjusted Term SOFR Rate (as defined in the Delayed Draw Term Loan Agreement) plus an applicable margin varying from 1.750% to 2.625% or (y) a base rate plus an applicable margin varying from 0.750% to 1.625%, in each case depending on the corporate family ratings of the Company from at least two of the Credit Rating Agencies. The Company will also pay an unused commitment fee on the Delayed Draw Term Loan Agreement of 0.200%.

The key covenants, limitations and requirements provided under Credit Agreement amendment noted above also apply to the Delayed Draw Term Loan Agreement.

As described in Note 2, *Recent Accounting Pronouncements*, the Company adopted ASU 2020-06 effective July 2, 2022, using a modified retrospective method, which resulted in the elimination of the originally recorded debt discount associated with the conversion feature on its 1.50% convertible notes due 2024.

Note 9. Pension and Other Post-Retirement Benefit Plans

The Company has pension and other post-retirement benefit plans in various countries. The Company's principal pension plans are in Japan, Thailand and the Philippines. All pension and other post-retirement benefit plans outside of the Company's Japan, Thailand and the Philippines defined benefit pension plans (the "Pension Plans") are immaterial to the Condensed Consolidated Financial Statements. The expected long-term rate of return on the Pension Plans assets is 2.5%.

Obligations and Funded Status

The following table presents the unfunded status of the benefit obligations for the Pension Plans:

	December 30, 2022	July 1, 2022
	(in millions)	
Benefit obligation at end of period	$ 302	$ 294
Fair value of plan assets at end of period	195	189
Unfunded status	$ 107	$ 105

The following table presents the unfunded amounts related to the Pension Plans as recognized on the Company's Condensed Consolidated Balance Sheets:

	December 30, 2022	July 1, 2022
	(in millions)	
Current liabilities	$ 1	$ 1
Non-current liabilities	106	104
Net amount recognized	$ 107	$ 105

Net periodic benefit costs were not material for the three and six months ended December 30, 2022.

Note 10. Related Parties and Related Commitments and Contingencies

Flash Ventures

The Company's business ventures with Kioxia Corporation ("Kioxia") consist of three separate legal entities: Flash Partners Ltd. ("Flash Partners"), Flash Alliance Ltd. ("Flash Alliance"), and Flash Forward Ltd. ("Flash Forward"), collectively referred to as "Flash Ventures".

The following table presents the notes receivable from, and equity investments in, Flash Ventures:

	December 30, 2022	July 1, 2022
	(in millions)	
Notes receivable, Flash Partners	$ 12	$ 27
Notes receivable, Flash Alliance	66	55
Notes receivable, Flash Forward	737	793
Investment in Flash Partners	174	166
Investment in Flash Alliance	251	243
Investment in Flash Forward	117	112
Total notes receivable and investments in Flash Ventures	$ 1,357	$ 1,396

During the three and six months ended December 30, 2022 and December 31, 2021, the Company made net payments to Flash Ventures of $1.0 billion and $2.0 billion, and $1.1 billion and $2.3 billion, respectively, for purchased flash-based memory wafers and net loans.

The Company makes, or will make, loans to Flash Ventures to fund equipment investments for new process technologies and additional wafer capacity. The Company aggregates its Flash Ventures' notes receivable into one class of financing receivables due to the similar ownership interest and common structure in each Flash Venture entity. For all reporting periods presented, no loans were past due and no loan impairments were recorded. The Company's notes receivable from each Flash Ventures entity, denominated in Japanese yen, are secured by equipment owned by that Flash Ventures entity.

As of December 30, 2022 and July 1, 2022, the Company had accounts payable balances due to Flash Ventures of $368 million and $320 million, respectively.

The Company's maximum reasonably estimable loss exposure (excluding lost profits) as a result of its involvement with Flash Ventures, based upon the Japanese yen to U.S. dollar exchange rate at December 30, 2022, is presented below. Investments in Flash Ventures are denominated in Japanese yen, and the maximum estimable loss exposure excludes any cumulative translation adjustment due to revaluation from the Japanese yen to the U.S. dollar.

	December 30, 2022
	(in millions)
Notes receivable	$ 815
Equity investments	542
Operating lease guarantees	1,895
Inventory and prepayments	1,128
Maximum estimable loss exposure	$ 4,380

The Company is obligated to pay for variable costs incurred in producing its share of Flash Ventures' flash-based memory wafer supply, based on its three-month forecast, which generally equals 50% of Flash Ventures' output. In addition, the Company is obligated to pay for half of Flash Ventures' fixed costs regardless of the output the Company chooses to purchase. The Company is not able to estimate its total wafer purchase commitment obligation beyond its rolling three-month purchase commitment because the price is determined by reference to the future cost of producing the semiconductor wafers. In addition, the Company is committed to fund 49.9% to 50.0% of each Flash Ventures entity's capital investments to the extent that each Flash Ventures entity's operating cash flow is insufficient to fund these investments.

In January 2022, the Company entered into additional agreements regarding Flash Ventures' investment in a new wafer fabrication facility currently under construction in Yokkaichi, Japan, referred to as "Y7". The primary purpose of Y7 is to provide clean room space to continue the transition of existing flash-based wafer capacity to newer flash technology nodes. The Company is committed to pay, among other items, future building depreciation prepayments aggregating approximately $147 million as follows: $124 million for the remaining six months of 2023 and $23 million in 2024, to be credited against future wafer charges.

Inventory Purchase Commitments with Flash Ventures. Purchase orders placed under Flash Ventures for up to three months are binding and cannot be canceled.

Research and Development Activities. The Company participates in common research and development ("R&D") activities with Kioxia and is contractually committed to a minimum funding level. R&D commitments are immaterial to the Condensed Consolidated Financial Statements.

Off-Balance Sheet Liabilities

Flash Ventures sells to and leases back from a consortium of financial institutions a portion of its tools and has entered into equipment lease agreements of which the Company guarantees half or all of the outstanding obligations under each lease agreement. The lease agreements are subject to customary covenants and cancellation events related to Flash Ventures and each of the guarantors. The occurrence of a cancellation event could result in an acceleration of Flash Ventures' obligations and a call on the Company's guarantees.

The following table presents the Company's portion of the remaining guarantee obligations under the Flash Ventures' lease facilities in both Japanese yen and U.S. dollar-equivalent, based upon the Japanese yen to U.S. dollar exchange rate as of December 30, 2022.

	Lease Amounts	
	(Japanese yen, in billions)	*(U.S. dollar, in millions)*
Total guarantee obligations	¥ 250	$ 1,895

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The following table details the breakdown of the Company's remaining guarantee obligations between the principal amortization and the purchase option exercise price at the end of the term of the Flash Ventures lease agreements, in annual installments as of December 30, 2022 in U.S. dollars, based upon the Japanese yen to U.S. dollar exchange rate as of December 30, 2022:

Annual Installments	Payment of Principal Amortization	Purchase Option Exercise Price at Final Lease Terms	Guarantee Amount
		(in millions)	
Remaining six months of 2023	$ 285	$ 55	$ 340
2024	450	99	549
2025	250	90	340
2026	261	136	397
2027	81	116	197
2028 and thereafter	12	60	72
Total guarantee obligations	$ 1,339	$ 556	$ 1,895

The Company and Kioxia have agreed to mutually contribute to, and indemnify each other and Flash Ventures for, environmental remediation costs or liability resulting from Flash Ventures' manufacturing operations in certain circumstances. The Company has not made any indemnification payments, nor recorded any indemnification receivables, under any such agreements. As of December 30, 2022, no amounts have been accrued in the Condensed Consolidated Financial Statements with respect to these indemnification agreements.

Unis Venture

The Company has a joint venture with Unisplendour Corporation Limited and Unissoft (Wuxi) Group Co. Ltd. ("Unis"), referred to as the "Unis Venture", to market and sell the Company's products in China and to develop data storage systems for the Chinese market in the future. The Unis Venture is 49% owned by the Company and 51% owned by Unis. The Company accounts for its investment in the Unis Venture under the equity method of accounting. Revenue on products distributed by the Unis Venture is recognized upon sell through to third-party customers. For both the three and six months ended December 30, 2022, the Company recognized approximately 3% of its consolidated revenue on products distributed by the Unis Venture. For both the three and six months ended December 31, 2021, the Company recognized approximately 4% of its consolidated revenue on products distributed by the Unis Venture. The outstanding accounts receivable due from the Unis Venture were 7% and 5% of Accounts receivable, net as of December 30, 2022 and July 1, 2022, respectively.

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Note 11. Leases and Other Commitments

Leases

The Company leases certain domestic and international facilities and data center space under long-term, non-cancelable operating leases that expire at various dates through 2034. These leases include no material variable or contingent lease payments. Operating lease assets and liabilities are recognized based on the present value of the remaining lease payments discounted using the Company's incremental borrowing rate. Operating lease assets also include prepaid lease payments minus any lease incentives. Extension or termination options present in the Company's lease agreements are included in determining the right-of-use asset and lease liability when it is reasonably certain the Company will exercise those options. Lease expense is recognized on a straight-line basis over the lease term. The following table summarizes supplemental balance sheet information related to operating leases as of December 30, 2022:

	Lease Amounts
	($ in millions)
Minimum lease payments by year:	
Remaining six months of 2023	$ 24
2024	47
2025	44
2026	43
2027	39
Thereafter	147
Total future minimum lease payments	344
Less: Imputed interest	54
Present value of lease liabilities	290
Less: Current portion (included in Accrued expenses)	39
Long-term operating lease liabilities (included in Other liabilities)	$ 251
Operating lease right-of-use assets (included in Other non-current assets)	$ 271
Weighted average remaining lease term in years	8.1
Weighted average discount rate	4.1 %

The following table summarizes supplemental disclosures of operating cost and cash flow information related to operating leases:

	Three Months Ended		Six Months Ended	
	December 30, 2022	December 31, 2021	December 30, 2022	December 31, 2021
	(in millions)			
Cost of operating leases	$ 14	$ 14	$ 28	$ 27
Cash paid for operating leases	12	12	26	24
Operating lease assets obtained in exchange for operating lease liabilities	—	11	4	123

Purchase Agreements and Other Commitments

In the normal course of business, the Company enters into purchase orders with suppliers for the purchase of components used to manufacture its products. These purchase orders generally cover forecasted component supplies needed for production during the next quarter, are recorded as a liability upon receipt of the components, and generally may be changed or canceled at any time prior to shipment of the components. The Company also enters into long-term agreements with suppliers that contain fixed future commitments, which are contingent on certain conditions such as performance, quality and technology of the vendor's components. As of December 30, 2022, the Company had the following minimum long-term commitments:

	Long-Term Commitments
	(in millions)
Year:	
Remaining six months of 2023	$ 193
2024	256
2025	180
2026	53
2027	46
Thereafter	150
Total	$ 878

Note 12. Shareholders' Equity

Stock-based Compensation Expense

The following tables present the Company's stock-based compensation for equity-settled awards by type (i.e., restricted stock units ("RSUs"), restricted stock unit awards with performance conditions or market conditions ("PSUs"), and rights to purchase shares of common stock under the Company's Employee Stock Purchase Plan ("ESPP")) and financial statement line as well as the related tax benefit included in the Company's Condensed Consolidated Statements of Operations:

	Three Months Ended		Six Months Ended	
	December 30, 2022	December 31, 2021	December 30, 2022	December 31, 2021
	(in millions)			
RSUs and PSUs	$ 79	$ 78	$ 154	$ 145
ESPP	7	9	18	18
Total	$ 86	$ 87	$ 172	$ 163

	Three Months Ended		Six Months Ended	
	December 30, 2022	December 31, 2021	December 30, 2022	December 31, 2021
	(in millions)			
Cost of revenue	$ 12	$ 14	$ 26	$ 23
Research and development	40	43	79	83
Selling, general and administrative	34	30	67	57
Subtotal	86	87	172	163
Tax benefit	(11)	(13)	(24)	(28)
Total	$ 75	$ 74	$ 148	$ 135

Windfall tax benefits and tax deficiencies for shortfalls related to the vesting and exercise of stock-based awards, which are recognized as a component of the Company's Income tax expense, were not material for the periods presented.

Compensation cost related to unvested RSUs, PSUs, and rights to purchase shares of common stock under the ESPP will generally be amortized on a straight-line basis over the remaining average service period. The following table presents the unamortized compensation cost and weighted average service period of all unvested outstanding awards as of December 30, 2022:

	Unamortized Compensation Costs	Weighted Average Service Period
	(in millions)	*(years)*
RSUs and PSUs [(1)]	$ 571	2.4
ESPP	89	1.9
Total unamortized compensation cost	$ 660	

(1) Weighted average service period assumes the performance metrics are met for the PSUs.

Plan Activities

Stock Options

The following table summarizes stock option activity under the Company's incentive plans. All outstanding options were exercisable at December 30, 2022:

	Number of Shares	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Life
	(in millions)		*(in years)*
Options outstanding at July 1, 2022	0.9	$ 66.76	0.54
Canceled or expired	(0.5)	83.50	
Options outstanding at December 30, 2022	0.4	$ 44.63	0.57

RSUs and PSUs

The following table summarizes RSU and PSU activity under the Company's incentive plans:

	Number of Shares	Weighted Average Grant Date Fair Value	Aggregate Intrinsic Value at Vest Date
	(in millions)		*(in millions)*
RSUs and PSUs outstanding at July 1, 2022	15.4	$ 52.89	
Granted	4.7	43.34	
Vested	(4.7)	53.76	$ 200
Forfeited	(0.9)	58.54	
RSUs and PSUs outstanding at December 30, 2022	14.5	$ 49.18	

RSUs and PSUs are generally settled in an equal number of shares of the Company's common stock at the time of vesting of the units.

Stock Repurchase Program

The Company's Board of Directors has authorized a stock repurchase program for the repurchase of up to $5.0 billion of the Company's common stock, which authorization is effective through July 25, 2023. The Company did not make any stock repurchases during the six months ended December 30, 2022 and has not repurchased any shares of its common stock pursuant to its stock repurchase program since the first quarter of fiscal 2019. Although the Company will reevaluate the repurchasing of common stock when appropriate, there can be no assurance if, when or at what level the Company may resume such activity. The remaining amount available to be repurchased under the Company's current stock repurchase program as of December 30, 2022 was $4.5 billion. Repurchases under the stock repurchase program may be made in the open market or in privately negotiated transactions and may be made under a Rule 10b5-1 plan.

Note 13. Income Tax Expense

The Tax Cuts and Jobs Act (the “2017 Act”), enacted on December 22, 2017, includes a broad range of tax reform proposals affecting businesses. The Company completed its accounting for the tax effects of the enactment of the 2017 Act during the second quarter of fiscal 2019. However, the U.S. Treasury and the Internal Revenue Service (“IRS”) have issued tax guidance on certain provisions of the 2017 Act since the enactment date, and the Company anticipates the issuance of additional regulatory and interpretive guidance. The Company applied a reasonable interpretation of the 2017 Act along with the then-available guidance in finalizing its accounting for the tax effects of the 2017 Act. Any additional regulatory or interpretive guidance would constitute new information, which may require further refinements to the Company’s estimates in future periods.

On August 16, 2022, President Biden signed into law the Inflation Reduction Act of 2022, which contained significant law changes related to tax, climate, energy, and health care. The tax measures include, among other things, a corporate alternative minimum tax of 15% on corporations with three-year average annual adjusted financial statement income exceeding $1 billion. The corporate alternative minimum tax will not be effective for the Company until fiscal year 2024 and the Company is currently evaluating the potential effects of these legislative changes.

The following table presents the Company’s Income tax expense and the effective tax rate:

	Three Months Ended		Six Months Ended	
	December 30, 2022	December 31, 2021	December 30, 2022	December 31, 2021
	($ in millions)			
Income (loss) before taxes	$ (385)	$ 646	$ (301)	$ 1,350
Income tax expense	61	82	118	176
Effective tax rate	(16)%	13 %	(39)%	13 %

Beginning in fiscal year 2023, the 2017 Act requires the Company to capitalize and amortize R&D expenses rather than expensing them in the year incurred. The tax effects related to the capitalization of R&D expenses are included in the effective tax rate for the three and six months ended December 30, 2022 but did not have a material impact on the effective tax rate. The primary drivers of the difference between the effective tax rate for the three and six months ended December 30, 2022 and the U.S. Federal statutory rate of 21% are the relative mix of earnings and losses by jurisdiction, the deduction for foreign derived intangible income, credits, and tax holidays in Malaysia, the Philippines and Thailand that will expire at various dates during fiscal years 2024 through 2031.

The primary drivers of the difference between the effective tax rate for the three and six months ended December 31, 2021 and the U.S. Federal statutory rate of 21% are the relative mix of earnings and losses by jurisdiction, the deduction for foreign derived intangible income, credits, and tax holidays in Malaysia, the Philippines and Thailand that will expire at various dates during fiscal years 2024 through 2031. In addition, the effective tax rate for the three and six months ended December 31, 2021 included the discrete effect of an increase to unrecognized tax benefits of $8 million and $25 million, respectively, as a result of ongoing discussions with various taxing authorities.

Uncertain Tax Positions

With the exception of certain unrecognized tax benefits that are directly associated with the tax position taken, unrecognized tax benefits are presented gross in the Condensed Consolidated Balance Sheets.

WESTERN DIGITAL CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

The following is a tabular reconciliation of the total amounts of unrecognized tax benefits excluding accrued interest and penalties for the three months ended December 30, 2022 (in millions):

Accrual balance at July 1, 2022	$	1,047
Gross increases related to current year tax positions		4
Gross increases related to prior year tax positions		11
Gross decreases related to prior year tax positions		(12
Settlements		(5
Lapse of statute of limitations		(3
Accrual balance at December 30, 2022	$	1,042

As of December 30, 2022, the liability for unrecognized tax benefits (excluding accrued interest and penalties) was $1.04 billion. Interest and penalties related to unrecognized tax benefits are recognized in liabilities recorded for uncertain tax positions and are recorded in the provision for income taxes. Accrued interest and penalties included in the Company's liability related to unrecognized tax benefits as of December 30, 2022 was $279 million. Of these amounts, approximately $1.18 billion could result in potential cash payments.

As previously disclosed, the IRS issued statutory notices of deficiency and notices of proposed adjustments with respect to transfer pricing with the Company's foreign subsidiaries and intercompany payable balances for years 2008 through 2015. In September 2018 and March 2019, the Company filed petitions with the U.S. Tax Court covering years 2008 through 2012, for which it had received statutory notices of deficiency, while years 2013 through 2015 remain in the jurisdiction of the IRS's Examination function. The IRS has filed various Amendments to Answer with the U.S. Tax Court which, together with the notices of proposed adjustments, would result in additional federal income tax liabilities totaling approximately $1.6 billion and penalties totaling $449 million with respect to years 2008 through 2015. In May 2022, the Company and the IRS tentatively reached a settlement for resolving the statutory notices of deficiency and notices of proposed adjustments with respect to years 2008 through 2015 subject to the parties entering into final stipulations and a closing agreement. Based on the tentative settlement for resolution, the Company expects to pay tax and interest totaling approximately $720 million to $760 million, which the Company expects to be partially offset by future reductions to its mandatory deemed repatriation tax obligations and tax savings from interest deductions aggregating to approximately $100 million to $150 million. While the Company continues to work with the IRS to come to a final agreement on the federal tax and interest calculations, the Company is uncertain as to when a final agreement will be reached and the exact timing of when any payments will be made. However, the Company believes it is reasonably likely that these payments may be made within the next twelve months and has classified that portion of these unrecognized tax benefits, including interest in Income taxes payable on its Condensed Consolidated Balance Sheets as of December 30, 2022. This classification and amount may be subject to change in the next twelve months depending on when the Company is able to reach a final agreement with the IRS.

The Company believes that adequate provision has been made for any adjustments that may result from any other tax examinations. However, the outcome of such tax examinations cannot be predicted with certainty. If any issues addressed in the Company's tax examinations are resolved in a manner not consistent with management's expectations, the Company could be required to adjust its provision for income taxes in the period such resolution occurs. Any significant change in the amount of the Company's liability for unrecognized tax benefits would most likely result from additional information or settlements relating to the examination of the Company's tax returns.

Note 14. Net Income (Loss) Per Common Share

The following table presents the computation of basic and diluted income (loss) per common share:

	Three Months Ended		Six Months Ended	
	December 30, 2022	December 31, 2021	December 30, 2022	December 31, 2021
	(in millions, except per share data)			
Net income (loss)	$ (446)	$ 564	$ (419)	$ 1,174
Weighted average shares outstanding:				
Basic	318	312	317	311
Employee stock options, RSUs, PSUs, and ESPP	—	3	—	4
Basic and diluted	318	315	317	315
Income (loss) per common share				
Basic	$ (1.40)	$ 1.81	$ (1.32)	$ 3.77
Diluted	$ (1.40)	$ 1.79	$ (1.32)	$ 3.73
Anti-dilutive potential common shares excluded	15	5	15	3

The Company computes basic income (loss) per common share using Net income (loss) and the weighted average number of common shares outstanding during the period. Diluted income (loss) per common share is computed using Net income (loss) and the weighted average number of common shares and potentially dilutive common shares outstanding during the period. Potentially dilutive common shares include dilutive outstanding employee stock options, RSUs and PSUs, and rights to purchase shares of common stock under the Company's ESPP. For the three and six months ended and December 31, 2021, the Company excluded common shares subject to certain outstanding equity awards from the calculation of diluted shares because their impact would have been anti-dilutive based on the Company's average stock price during the period. For the three and six months ended December 30, 2022, the Company recorded a net loss and all shares subject to outstanding equity awards were excluded from the calculation of diluted shares for those periods because their impact would have been anti-dilutive.

Note 15. Employee Termination, Asset Impairment, and Other Charges

Business Realignment

The Company periodically incurs charges as part of the integration process of recent acquisitions and to realign its operations with anticipated market demand, primarily consisting of organization rationalization designed to streamline its business, reduce its cost structure and focus its resources. The Company recorded the following charges related to these actions:

	Three Months Ended		Six Months Ended	
	December 30, 2022	December 31, 2021	December 30, 2022	December 31, 2021
	(in millions)			
Employee termination benefits	$ 61	$ 3	$ 85	$ 18
Asset impairments and losses on disposal of assets	15	(1)	15	2
Total employee termination, asset impairment, and other charges	$ 76	$ 2	$ 100	$ 20

The following table presents an analysis of the components of these activities against the reserve during the six months ended December 30, 2022:

	Employee Termination Benefits
	(in millions)
Accrual balance at July 1, 2022	$ 17
Charges	85
Cash payments	(69)
Accrual balance at December 30, 2022	$ 33

Note 16. Legal Proceedings

Tax

For disclosures regarding statutory notices of deficiency issued by the IRS on June 28, 2018 and December 10, 2018, petitions filed by the Company with the U.S. Tax Court in September 2018 and March 2019, additional penalties asserted by the IRS in March 2021 and further Amendments to Answers filed by the IRS in June 2021 and January 2022, and a tentative resolution with respect to certain matters, see Note 13, *Income Tax Expense*.

Other Matters

In the normal course of business, the Company is subject to legal proceedings, lawsuits and other claims. Although the ultimate aggregate amount of probable monetary liability or financial impact with respect to these other matters is subject to many uncertainties, management believes that any monetary liability or financial impact to the Company from these matters, individually and in the aggregate, would not be material to the Company's financial condition, results of operations or cash flows. However, any monetary liability and financial impact to the Company from these matters could differ materially from the Company's expectations.

Note 17. Subsequent Events

On January 31, 2023, the Board of Directors of the Company authorized the designation of 900,000 shares of Series A Convertible Perpetual Preferred Stock, par value $0.01 per share (the “Preferred Shares”) from the Company’s existing five million authorized but unissued shares of preferred stock and issued the Preferred Shares through a private placement for an aggregate purchase price of $900 million. The Preferred Shares will have a stated value of $1,000 per share and accrue a cumulative preferred dividend at an annual rate of 6.25% per annum (increasing to 7.25% per annum on January 31, 2030 and to 8.25% per annum on January 31, 2033) compounded on a quarterly basis. The Preferred Shares will also participate in any dividends declared for common shareholders on an as-converted equivalent basis. The Preferred Shares will be convertible into shares of the Company’s common stock at an initial conversion rate of $47.75 per share (the “Conversion Price”) (subject to anti-dilution adjustments and certain other one-time adjustments upon the occurrence of various specified spin-off transactions) applied to the aggregate of the stated value plus any cumulative accrued but unpaid dividends (the “Accumulated Stated Value”). In the event of a standalone spin-off transaction, the holders of Preferred Shares may have one third of their Preferred Shares converted to a similar class of preferred shares of the spin-off entity. The Preferred Shares will be convertible at the option of the holder beginning on January 31, 2024, or on the date a specified spin-off transaction is completed, if earlier. The Preferred Shares will be convertible at the option of the Company after January 31, 2026 if the closing price per share of the Company’s common stock exceeds 150% of the Conversion Price for at least 20 out of 30 consecutive trading days. After January 31, 2030, the Company will have the right, but not the obligation, to redeem the Preferred Shares at an amount equal to 110% of the Accumulated Stated Value. Redemption is contingently mandatory in the event of a fundamental change in the business as defined in the designation of the Preferred Shares. The Preferred Shares will vote on an as-converted equivalent basis along with holders of the Company’s common stock, except to the extent that shares issuable upon conversion of the Preferred Stock would exceed 19.9% of common stock outstanding immediately prior to the original issuance date of the Preferred Stock. In the event of liquidation, holders of the Preferred Shares will be senior to the holders of the Company’s common stock.

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

The following discussion and analysis contains forward-looking statements within the meaning of the federal securities laws, and should be read in conjunction with the disclosures we make concerning risks and other factors that may affect our business and operating results. You should read this information in conjunction with the unaudited Condensed Consolidated Financial Statements and the notes thereto included in this Quarterly Report on Form 10-Q, and the audited Consolidated Financial Statements and notes thereto included in Part II, Item 8 of our Annual Report on Form 10-K for the fiscal year ended July 1, 2022. See also "Forward-Looking Statements" immediately prior to Part I, Item 1 in this Quarterly Report on Form 10-Q.

Unless otherwise indicated, references herein to specific years and quarters are to our fiscal years and fiscal quarters. As used herein, the terms "we," "us," "our," and the "Company" refer to Western Digital Corporation and its subsidiaries.

Our Company

We are on a mission to unlock the potential of data by harnessing the possibility to use it. We are a leading developer, manufacturer, and provider of data storage devices based on both flash-based products ("Flash") and hard disk drives ("HDD") technologies. With dedicated business units driving advancements in NAND flash and magnetic recording technologies, we create and drive innovations needed to help customers capture, preserve, access, and transform an ever-increasing diversity of data.

Our fiscal year ends on the Friday nearest to June 30 and typically consists of 52 weeks. Approximately every five to six years, we report a 53-week fiscal year to align the fiscal year with the foregoing policy. Fiscal years 2023, which ends on June 30, 2023, and 2022, which ended on July 1, 2022, are each comprised of 52 weeks, with all quarters presented consisting of 13 weeks.

Key Developments

Strategic Alternatives

In June 2022, we announced that we are reviewing potential strategic alternatives aimed at further optimizing long-term value for stockholders. The Executive Committee of our Board of Directors is overseeing the assessment process and evaluating a range of alternatives, including options for separating our Flash and HDD business units. As of December 30, 2022, we are still actively working with our financial advisors and our legal counsel in this strategic review process.

Operational and COVID-19 Pandemic Update

Macroeconomic factors such as inflation, higher interest rates and recession concerns have softened demand for our products, with certain customers reducing purchases as they adjust their production levels and right-size their inventories. As a result, we and our industry are experiencing a supply-demand imbalance, which has resulted in reduced shipments and negatively impacted pricing, particularly in Flash. We expect the market pressures on Flash pricing to continue for the next few quarters. Since the beginning of fiscal 2023, we have scaled back on capital expenditures, consolidated production lines and reduced bit growth to align with market demand and implemented measures to reduce operating expenses. This has resulted in incremental charges for Employee termination, asset impairment and other charges and manufacturing underutilization charges in HDD in the second quarter of 2023 and may impact near-term results. In addition, we have reduced wafer starts for Flash by 30% as of January 2023 and expect underutilization charges for that business unit to impact near-term results. However, we believe digital transformation will continue to drive long-term growth for data storage in both Flash and HDD and believe that the actions we are taking will position us for more profitable growth as supply and demand levels begin to balance.

We believe we have made significant progress in strengthening our product portfolio to meet our customers' growing and evolving storage needs. Our BiCS5 based products continue to play a significant role in driving top line results across our end markets. Additionally, hard drive products utilizing OptiNAND and shingled magnetic recording ("SMR") technologies have commenced commercial shipments and our latest 26-terabyte SMR drives are undergoing qualifications at multiple cloud and OEM customers. We continued commercial shipment of consumer flash devices based on our next generation 3D-flash technology and are beginning productization of BiCS8, which incorporates new 3D-NAND architectural innovations to deliver improved performance and cost-effectiveness. We are aware of the ongoing trends in the HDD Client market as PCs shift from using HDD to Flash technology and as a result, we have and are still undergoing actions to restructure our HDD manufacturing footprint to reflect this market dynamic, including a sharp reduction in our client hard drive production capacity.

The COVID-19 environment has begun to normalize. The responses to COVID-19 taken by ourselves and others in the supply chain contributed to increases in the costs of their services which in turn impacted our operations, but these costs have now largely been normalized in our operating results.

We will continue to actively monitor recent developments impacting our business and may take additional responsive actions that we determine to be in the best interests of our business and stakeholders. See "Adverse global or regional conditions could harm our business," "Public health crises, including the COVID-19 pandemic, have had, and could in the future, have a negative effect on our business" and "We are dependent on a limited number of qualified suppliers who provide critical services, materials or components, and a disruption in our supply chain could negatively affect our business" in Part I, Item 1A, *Risk Factors*, of our Annual Report on Form 10-K for the year ended July 1, 2022 for more information regarding the risks we face as a result of macroeconomic conditions, the COVID-19 pandemic and supply chain disruptions.

Financing Activities

In December 2022, we amended the loan agreement governing our revolving credit facility and Term Loan A-2 to modify the leverage ratio requirements of our financial covenant through our quarter ending September 27, 2024 to provide additional financial flexibility as we navigate through the current dynamic economic environment. The amendment also accelerates the due date for amounts outstanding under the loan agreement from January 7, 2027 to November 2, 2023 if, as of that date, our cash and cash equivalents plus available unused capacity under our credit facilities does not exceed by $1 billion the sum of the outstanding balance of our 1.50% convertible notes due 2024 plus the outstanding principal amount of any other debt maturing within 12 months.

Subsequent to the end of the second quarter of 2023, on January 25, 2023, we entered into a new delayed draw term loan agreement, which allows us to draw a single unsecured loan of up to $875 million any time through June 30, 2023. Any amount drawn will be due 364 days after funding or such earlier date that conditions for acceleration of amounts due under the loan agreement have been triggered as described above. Also, on January 31, 2023, we issued an aggregate of 900,000 shares of Series A Preferred Stock for an aggregate purchase price of $900 million. We believe these transactions will provide us with greater financial flexibility to manage our business. Additional information regarding our indebtedness, including the principal repayment terms, interest rates, covenants and other key terms of our outstanding indebtedness, is included in Part I, Item 1, Note 8, *Debt*, of the Notes to Condensed Consolidated Financial Statements in this Quarterly Report on Form 10-Q and in Part II, Item 8, Note 8, *Debt*, of the Notes to Consolidated Financial Statements included in our Annual Report on Form 10-K for the fiscal year ended July 1, 2022. Additional information regarding the terms of our Series A Preferred Stock is included in Note 17, *Subsequent Events*, of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q.

Tax Resolution

As previously disclosed, we have received statutory notices of deficiency and notices of proposed adjustments from the Internal Revenue Service ("IRS") with respect to 2008 through 2015. During 2022, new information became available which required us to re-measure our unrecognized tax benefits for this IRS matter. Additionally, during 2022, we and the IRS tentatively reached a settlement for resolving this matter. Additional information regarding this tentative settlement and our assessment of the potential tax and interest payments we expect to pay in connection with the settlement is provided in our discussion of Income tax expense in our results of operations below, as well as in Part I, Item 1, Note 13, *Income Tax Expense*, of the Notes to the Condensed Consolidated Financial Statements, and in the "Short- and Long-Term Liquidity-Unrecognized Tax Benefits" section below.

Russia Sanctions

In February 2022, the U.S. and other countries imposed sanctions on Russia. In accordance with these sanctions, we have ceased shipments to distributors for customers located in Russia. Our revenue from distributors for customers in Russia have not been significant. We have no material assets or operations in Russia.

Results of Operations

Second Quarter and First Half Overview

The following table sets forth, for the periods presented, selected summary information from our Condensed Consolidated Statements of Operations by dollars and percentage of net revenue[1]:

	Three Months Ended					
	December 30, 2022		December 31, 2021		$ Change	% Change
	$ in millions					
Revenue, net	$ 3,107	100.0 %	$ 4,833	100.0 %	$ (1,726)	(36) %
Cost of revenue	2,579	83.0	3,250	67.2	(671)	(21)
Gross profit	528	17.0	1,583	32.8	(1,055)	(67)
Operating expenses:						
Research and development	523	16.8	575	11.9	(52)	(9)
Selling, general and administrative	250	8.0	279	5.8	(29)	(10)
Employee termination, asset impairment, and other charges	76	2.4	2	—	74	3,700
Total operating expenses	849	27.3	856	17.7	(7)	(1)
Operating income (loss)	(321)	(10.3)	727	15.0	(1,048)	(144)
Interest and other income (expense):						
Interest income	3	0.1	1	—	2	200
Interest expense	(73)	(2.3)	(76)	(1.6)	3	(4)
Other income (expense), net	6	0.2	(6)	(0.1)	12	(200)
Total interest and other expense, net	(64)	(2.1)	(81)	(1.7)	17	(21)
Income (loss) before taxes	(385)	(12.4)	646	13.4	(1,031)	(160)
Income tax expense	61	2.0	82	1.7	(21)	(26)
Net income (loss)	$ (446)	(14.4)%	$ 564	11.7 %	$ (1,010)	(179) %

(1) Percentages may not total due to rounding.

	Six Months Ended					
	December 30, 2022		December 31, 2021		$ Change	% Change
	$ in millions					
Revenue, net	$ 6,843	100.0 %	$ 9,884	100.0 %	$ (3,041)	(31) %
Cost of revenue	5,334	77.9	6,636	67.1	(1,302)	(20)
Gross profit	1,509	22.1	3,248	32.9	(1,739)	(54)
Operating expenses:						
Research and development	1,075	15.7	1,153	11.7	(78)	(7)
Selling, general and administrative	497	7.3	570	5.8	(73)	(13)
Employee termination, asset impairment, and other charges	100	1.5	20	0.2	80	400
Total operating expenses	1,672	24.4	1,743	17.6	(71)	(4)
Operating income (loss)	(163)	(2.4)	1,505	15.2	(1,668)	(111)
Interest and other income (expense):						
Interest income	5	0.1	3	—	2	67
Interest expense	(143)	(2.1)	(154)	(1.6)	11	(7)
Other income (expense), net	—	—	(4)	—	4	(100)
Total interest and other expense, net	(138)	(2.0)	(155)	(1.6)	17	(11)
Income (loss) before taxes	(301)	(4.4)	1,350	13.7	(1,651)	(122)
Income tax expense	118	1.7	176	1.8	(58)	(33)
Net income (loss)	$ (419)	(6.1)%	$ 1,174	11.9 %	$ (1,593)	(136) %

(1) Percentages may not total due to rounding.

The following table sets forth, for the periods presented, a summary of our segment information:

	Three Months Ended		Six Months Ended	
	December 30, 2022	December 31, 2021	December 30, 2022	December 31, 2021
	$ in millions			
Net revenue:				
Flash	$ 1,657	$ 2,620	$ 3,379	$ 5,110
HDD	1,450	2,213	3,464	4,774
Total net revenue	$ 3,107	$ 4,833	$ 6,843	$ 9,884
Gross profit:				
Flash	$ 240	$ 946	$ 662	$ 1,867
HDD	300	677	874	1,469
Unallocated corporate items:				
Stock-based compensation expense	(12)	(14)	(26)	(23)
Amortization of acquired intangible assets	—	(26)	(1)	(65)
Total unallocated corporate items	(12)	(40)	(27)	(88)
Consolidated gross profit	$ 528	$ 1,583	$ 1,509	$ 3,248
Gross margin:				
Flash	14.5 %	36.1 %	19.6 %	36.5 %
HDD	20.7 %	30.6 %	25.2 %	30.8 %
Consolidated gross margin	17.0 %	32.8 %	22.1 %	32.9 %

The following table sets forth for the periods presented, summary information regarding our disaggregated revenue:

	Three Months Ended		Six Months Ended	
	December 30, 2022	December 31, 2021	December 30, 2022	December 31, 2021
	($ in millions)			
Revenue by End Market				
Cloud	$ 1,224	$ 1,920	$ 3,053	$ 4,145
Client	1,089	1,854	2,318	3,707
Consumer	794	1,059	1,472	2,032
Total Revenue	$ 3,107	$ 4,833	$ 6,843	$ 9,884
Revenue by Geography				
Asia	$ 1,494	$ 2,610	$ 3,180	$ 5,285
Americas	1,090	1,407	2,513	3,021
Europe, Middle East and Africa	523	816	1,150	1,578
Total Revenue	$ 3,107	$ 4,833	$ 6,843	$ 9,884

Comparison of Three and Six Months Ended December 30, 2022 to Three and Six Months Ended December 31, 2021

Net Revenue

The decrease in consolidated net revenue for the three and six months ended December 30, 2022 from the comparable periods in the prior year reflected decreases in exabytes sold primarily in HDD, as certain customers reduced purchases as they adjusted their production levels and right-sized their inventories and also reflected lower average selling prices primarily in Flash. These items are further discussed below in our discussion by segment.

Flash revenue decreased 37% and 34% for the three and six months ended December 30, 2022, respectively from the comparable periods in the prior year. The decline was primarily driven by a decline in average selling prices per gigabyte caused by a supply-demand imbalance, which was exacerbated by the current macroeconomic environment.

HDD revenue decreased 34% for the three months ended December 30, 2022 from the comparable period in the prior year, substantially all of which was driven by a decrease in exabytes sold. The decline in exabytes sold was primarily driven by customers primarily in our Cloud and to a lesser extent in Client and Consumer end markets due to the macroeconomic pressures noted in “Operational and COVID-19 Pandemic Update” above and our end customers right-sizing their inventories. HDD revenue decreased 27% for the six months ended December 30, 2022 from the comparable period in the prior year, primarily driven by a 22% decrease in exabytes sold as well as a decrease in the average price per gigabyte. The decrease in exabytes sold for the six-month period was largely attributable to the same factors noted above for the three-month period with pricing per gigabyte impacted by a higher mix of enterprise drives.

The decrease in Cloud revenue for the three months ended December 30, 2022 from the comparable period in the prior year reflected a decline in capacity enterprise drives sold to U.S. cloud customers, as they reduced purchases to right-size their inventories. In Client, the decrease in revenue for the three months ended December 30, 2022 from the comparable period in the prior year was primarily driven by the decline in average selling price per gigabyte in Flash and, to a lesser extent, a decline in client SSD shipments for PC applications. In Consumer, the decrease in revenue for the three months ended December 30, 2022 from the comparable period in the prior year primarily reflected the decrease in average selling price per gigabyte in Flash and to a lesser extent, a decline in retail HDD shipments.

The decreases in Cloud and Consumer revenue for the six months ended December 30, 2022 from the comparable period in the prior year primarily reflected the same drivers noted above for the three-month period, respectively. In Client, the decrease in revenue for the six months ended December 30, 2022 from the comparable period in the prior year primarily reflected a decline in average selling price per gigabyte in Flash and, to a lesser extent, a decline in both Flash and HDD shipments for PC applications, due to lower demand as a result of macroeconomic pressures.

The changes in net revenue by geography for the three and six months ended December 30, 2022 from the comparable periods in the prior year reflected a larger decline in Asia from lower Client revenue from OEMs in this region as they reduced purchases to align with current market demand, as well as routine variations in the mix of business.

Our top 10 customers accounted for 47% of our net revenue for the three months ended December 30, 2022, compared to 46% of our net revenue for the three months ended December 31, 2021. Our top 10 customers accounted for 48% of our net revenue for the six months ended December 30, 2022, compared to 44% of our net revenue for the six months ended December 31, 2021. For each of the three and six months ended December 30, 2022 and December 31, 2021, no single customer accounted for 10% or more of our net revenue.

Consistent with standard industry practice, we have sales incentive and marketing programs that provide customers with price protection and other incentives or reimbursements that are recorded as a reduction to gross revenue. These programs represented 18% of gross revenue for each period presented. The amounts attributed to our sales incentive and marketing programs generally vary according to several factors including industry conditions, list pricing strategies, seasonal demand, competitor actions, channel mix and overall availability of products. Changes in future customer demand and market conditions may require us to adjust our incentive programs as a percentage of gross revenue.

Gross Profit and Gross Margin

Consolidated gross profit decreased by $1.06 billion for the three months ended December 30, 2022 from the comparable period in the prior year, which reflects the impact from the decrease in revenue in both Flash and HDD as well as approximately $100 million of charges in the current period related to manufacturing underutilization in HDD. Consolidated gross margin decreased 15.8 percentage points for the three months ended December 30, 2022 from the comparable period in the prior year, which primarily reflects lower average price per gigabyte in Flash and the impact of the underutilization charges in HDD. Flash gross margin decreased by 21.6 percentage points year over year, primarily reflecting the lower average selling price per gigabyte. HDD gross margin decreased by 9.9 percentage points year over year, of which the underutilization charge reflected approximately 7 percentage points with the remainder primarily driven by lower economies of scale as we tempered production.

Consolidated gross profit decreased by $1.74 billion for the six months ended December 30, 2022 from the comparable period in the prior year, which reflects the decrease in revenue in both HDD and Flash and the approximate $100 million underutilization charge in HDD during the three months ended December 30, 2022, partially offset by a $64 million decrease during the six months ended December 30, 2022 in charges related to amortization expense on acquired intangible assets, some of which became fully amortized. Consolidated gross margin decreased 10.8 percentage points for the six months ended December 30, 2022 from the comparable period in the prior year, which reflects lower gross margin in both Flash and HDD and the underutilization charges noted above. Flash and HDD gross margin decreased by 16.9 and 5.6 percentage points year over year, respectively, reflecting the same factors noted above for the three-month period.

Operating Expenses

Research and development ("R&D") expense decreased $52 million and $78 million for the three and six months ended December 30, 2022, respectively, from the comparable periods in the prior year. The declines were primarily driven by a reduction in variable compensation expenses and material use as we took actions to reduce expenses in the current environment.

Selling, general and administrative ("SG&A") expense decreased $29 million and $73 million for the three and six months ended December 30, 2022, respectively, from the comparable periods in the prior year. The declines were primarily driven by a reduction in expenses related to outside services, variable compensation expenses, and material use as we took actions to reduce expenses in the current environment.

Employee termination, asset impairment and other charges increased $74 million and $80 million for the three and six months ended December 30, 2022, respectively, from the comparable periods in the prior year. The increases were due to restructuring actions taken to adjust our cost structure to align with the current demand environment. For information regarding Employee termination, asset impairment and other charges, see Part I, Item 1, Note 15, *Employee Termination, Asset Impairment, and Other Charges* of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q.

Interest and Other Income (Expense)

Total interest and other expense, net decreased $17 million for each of the three and six months ended December 30, 2022 from the comparable periods in the prior year reflecting lower foreign exchange losses and lower interest expense resulting from the pay-down of principal on our debt.

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Income Tax Expense

The Tax Cuts and Jobs Act (the "2017 Act") includes a broad range of tax reform proposals affecting businesses. We completed our accounting for the tax effects of the enactment of the 2017 Act during the second quarter of fiscal 2019. However, the U.S. Treasury and the Internal Revenue Service ("IRS") have issued tax guidance on certain provisions of the 2017 Act since the enactment date, and we anticipate the issuance of additional regulatory and interpretive guidance. We applied a reasonable interpretation of the 2017 Act along with the then-available guidance in finalizing our accounting for the tax effects of the 2017 Act. Any additional regulatory or interpretive guidance would constitute new information, which may require further refinements to our estimates in future periods.

On August 16, 2022, President Biden signed into law the Inflation Reduction Act of 2022, which contained significant law changes related to tax, climate, energy, and health care. The tax measures include, among other things, a corporate alternative minimum tax of 15% on corporations with three-year average annual adjusted financial statement income exceeding $1 billion. The corporate alternative minimum tax will not be effective for us until fiscal year 2024. We are currently evaluating the potential effects of these legislative changes.

The following table sets forth income tax information from our Condensed Consolidated Statements of Operations by dollar and effective tax rate:

	Three Months Ended		Six Months Ended	
	December 30, 2022	December 31, 2021	December 30, 2022	December 31, 2021
	$ in millions			
Income (loss) before taxes	$ (385)	$ 646	$ (301)	$ 1,350
Income tax expense	61	82	118	176
Effective tax rate	(16)%	13 %	(39)%	13 %

Beginning in fiscal year 2023, the 2017 Act requires us to capitalize and amortize R&D expenses rather than expensing them in the year incurred. The tax effects related to the capitalization of R&D expenses are included in the effective tax rate for the three and six months ended December 30, 2022, but did not have a material impact on our effective tax rate. The primary drivers of the difference between the effective tax rate for the three and six months ended December 30, 2022 and the U.S. Federal statutory rate of 21% are the relative mix of earnings and losses by jurisdiction, the deduction for foreign derived intangible income, credits, and tax holidays in Malaysia, the Philippines and Thailand that will expire at various dates during fiscal years 2024 through 2031.

The primary drivers of the difference between the effective tax rate for the three and six months ended December 31, 2021 and the U.S. Federal statutory rate of 21% are the relative mix of earnings and losses by jurisdiction, the deduction for foreign derived intangible income, credits, and tax holidays in Malaysia, the Philippines and Thailand that will expire at various dates during fiscal years 2024 through 2031. In addition, the effective tax rate for the three and six months ended December 31, 2021 included the discrete effect of an increase to unrecognized tax benefits of $8 million and $25 million, respectively, as a result of ongoing discussions with various taxing authorities.

Our future effective tax rate is subject to future regulatory developments and changes in the mix of our U.S. earnings compared to foreign earnings. The 2017 Act requires us to capitalize and amortize R&D expenses rather than expensing them in the year incurred. As described above, these capitalized expenses are included in our effective tax rate for the three and six months ended December 30, 2022, but did not have a material impact on the effective tax rate in those periods due to our reduced profitability. Mandatory capitalization of R&D is expected to materially increase our effective tax rate and taxes paid in future periods, if not repealed or otherwise modified. In addition, our total tax expense in future years may also vary as a result of discrete items such as excess tax benefits or deficiencies.

For additional information regarding Income tax expense, see Part I, Item 1, Note 13, *Income Tax Expense*, of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q.

Liquidity and Capital Resources

The following table summarizes our statements of cash flows:

	Six Months Ended	
	December 30, 2022	December 31, 2021
	(in millions)	
Net cash provided by (used in):		
Operating activities	$ 41	$ 1,187
Investing activities	(482)	(569)
Financing activities	(12)	(1,456)
Effect of exchange rate changes on cash	(3)	(1)
Net decrease in cash and cash equivalents	$ (456)	$ (839)

We and the IRS tentatively reached a basis for resolving the statutory notices of deficiency and notices of proposed adjustments with respect to fiscal years 2008 through 2015. We currently expect to pay tax and interest totaling approximately $720 million to $760 million, which we expect to be partially offset by future reductions to our mandatory deemed repatriation tax obligations and tax savings from interest deductions aggregating to approximately $100 million to $150 million. See Part I, Item 1, Note 13, *Income Tax Expense*, of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q for further details.

We have an existing shelf registration statement (the "Shelf Registration Statement") filed with the Securities and Exchange Commission that expires in August 2024, which allows us to offer and sell shares of common stock, preferred stock, warrants, and debt securities. We may use the Shelf Registration Statement or other capital sources, including other offerings of equity or debt securities or the credit markets, to satisfy future financing needs, including planned or unanticipated capital expenditures, investments, debt repayments or other expenses. Any such additional financing will be subject to market conditions and may not be available on terms acceptable to us or at all.

We believe our cash, cash equivalents and cash generated from operations as well as our available credit facilities, including the availability under our new delayed term loan agreement and the proceeds from the issuance of our Series A Preferred Stock as discussed in "Key Developments - Financing Activities", will be sufficient to satisfy our IRS obligation and meet our working capital, debt and capital expenditure needs for at least the next twelve months and for the foreseeable future thereafter. We believe we can also access the various debt capital markets to further supplement our liquidity position. Our ability to sustain our working capital position is subject to a number of risks that we discuss in Part I, Item 1A, *Risk Factors*, in our Annual Report on Form 10-K for the year ended July 1, 2022.

As noted previously, we are scaling back on capital expenditures and consolidating production lines and reducing bit growth to align with market demand. We are now reducing our expected expenditures for property, plant and equipment for our company plus our portion of the capital expenditures by our Flash Ventures joint venture with Kioxia for its operations from our previous estimate of an aggregate of $2.7 billion down to $2.3 billion for 2023. After consideration of the Flash Ventures' lease financing of its capital expenditures and net operating cash flow, we have reduced the expected net cash used for our purchases of property, plant and equipment and net activity in notes receivable relating to Flash Ventures from a cash outflow of $1.3 billion to an amount below $1 billion during 2023. The total expected cash to be used could vary depending on the timing and completion of various capital projects and the availability, timing and terms of related financing.

A total of $1.33 billion and $1.84 billion of our Cash and cash equivalents was held by our foreign subsidiaries as of December 30, 2022 and December 31, 2021, respectively. There are no material tax consequences that were not previously accrued for on the repatriation of this cash.

Our cash equivalents are primarily invested in money market funds that invest in U.S. Treasury securities and U.S. Government agency securities. In addition, from time to time, we also invest directly in certificates of deposit, asset backed securities and corporate and municipal notes and bonds.

Operating Activities

Cash flow from operating activities primarily consists of net income, adjusted for non-cash charges, plus or minus changes in operating assets and liabilities. This represents our principal source of cash. Net cash used for changes in operating assets and liabilities was $257 million for the six months ended December 30, 2022, as compared to $715 million for the six months ended December 31, 2021, which largely reflects the reduction in volume of our business. Changes in our operating assets and liabilities are largely affected by our working capital requirements, which are dependent on our volume of business and the effective management of our cash conversion cycle as well as timing of payments for taxes. Our cash conversion cycle measures how quickly we can convert our products into cash through sales. The cash conversion cycles were as follows (in days):

	Three Months Ended	
	December 30, 2022	December 31, 2021
Days sales outstanding	56	52
Days in inventory	133	102
Days payables outstanding	(55)	(68)
Cash conversion cycle	134	86

Changes in days sales outstanding (“DSO”) are generally due to the timing of shipments. Changes in days in inventory (“DIO”) are generally related to the timing of inventory builds, including staging of inventory to meet expected future demand. Changes in days payables outstanding (“DPO”) are generally related to production volume and the timing of purchases during the period. From time to time, we modify the timing of payments to our vendors. We make modifications primarily to manage our vendor relationships and to manage our cash flows, including our cash balances. Generally, we make the payment term modifications through negotiations with our vendors or by granting to, or receiving from, our vendors’ payment term accommodations.

For the three months ended December 30, 2022, DSO increased by 4 days from the comparable period in the prior year, primarily reflecting the timing of shipments and customer collections. DIO increased by 31 days from the comparable period in the prior year primarily reflecting a decline in products shipped. DPO decreased by 13 days from the comparable period in the prior year primarily due to reductions in capital expenditures and HDD production levels as well as routine variations in the timing of purchases and payments during the period. We have seen no significant deterioration in our receivables as a result of COVID-19 or other market conditions.

Investing Activities

Net cash used in investing activities for the six months ended December 30, 2022 primarily consisted of $578 million in capital expenditures partially offset by a $82 million net decrease in notes receivable issuances to Flash Ventures. Net cash used in investing activities for the six months ended December 31, 2021 primarily consisted of $551 million in capital expenditures and a $17 million net increase in notes receivable issuances to Flash Ventures.

Financing Activities

During the six months ended December 30, 2022, cash flows from financing activities primarily consisted of $55 million used for taxes paid on vested stock awards under employee stock plans, partially offset by $48 million from the issuance of stock under employee stock plans. In addition, we drew and repaid $1.18 billion under our revolving credit facility within the period. Cash used in financing activities for the six months ended December 31, 2021 primarily consisted of $2.43 billion for repayment of debt, as well as $80 million for taxes paid on vested stock awards under employee stock plans offset by proceeds of $998 million from the issuance of new debt, and $60 million from the issuance of stock under employee stock plans.

Off-Balance Sheet Arrangements

Other than the commitments related to Flash Ventures incurred in the normal course of business and certain indemnification provisions (see “Short and Long-term Liquidity-Purchase Obligations and Other Commitments” below), we do not have any other material off-balance sheet financing arrangements or liabilities, guarantee contracts, retained or contingent interests in transferred assets, or any other obligation arising out of a material variable interest in an unconsolidated entity. We do not have any majority-owned subsidiaries that are not included in the Condensed Consolidated Financial Statements. Additionally, with the exception of Flash Ventures and our joint venture with Unisplendour Corporation Limited and Unissoft (Wuxi) Group Co. Ltd., we do not have an interest in, or relationships with, any variable interest entities. For additional information regarding our off-balance sheet arrangements, see Part I, Item 1, Note 10, *Related Parties and Related Commitments and Contingencies*, of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q.

Short- and Long-term Liquidity

Material Cash Requirements

In addition to cash requirements for unrecognized tax benefits discussed below, the following is a summary of our known material cash requirements, including those for capital expenditures, as of December 30, 2022:

	Total	1 Year (Remaining Six Months of 2023)	2-3 Years (2024-2025)	4-5 Years (2026-2027)	More than 5 Years (Beyond 2027)
			(in millions)		
Long-term debt, including current portion[(1)]	$ 7,100	$ —	$ 1,363	$ 4,738	$ 999
Interest on debt	1,256	154	609	387	106
Flash Ventures related commitments[(2)]	5,274	1,950	2,545	913	(134)
Operating leases	344	24	91	82	147
Purchase obligations and other commitments	3,613	2,591	773	99	150
Mandatory Deemed Repatriation Tax	657	—	402	255	—
Total	$ 18,244	$ 4,719	$ 5,783	$ 6,474	$ 1,268

(1) Principal portion of debt, excluding discounts and issuance costs.

(2) Includes reimbursement for depreciation and lease payments on owned and committed equipment, funding commitments for loans and equity investments and payments for other committed expenses, including R&D and building depreciation. Funding commitments assume no additional operating lease guarantees. Additional operating lease guarantees can reduce funding commitments.

Debt

In addition to our existing debt, as of December 30, 2022, we had $2.25 billion available for borrowing under our revolving credit facility until January 2027, subject to customary conditions under the loan agreement. Furthermore, we entered into a delayed draw term loan agreement as noted in "Key Developments - Financing Activities" which provides us with an additional $875 million unsecured term loan available to borrow through June 30, 2023, subject to customary conditions and certain financial covenants under the loan agreement. The agreements governing these credit facilities each include limits on secured indebtedness and certain types of unsecured subsidiary indebtedness and require certain of our subsidiaries to provide guarantees to the extent the conditions providing for such guarantees are met. Additional information regarding our indebtedness, including information about principal repayment terms, interest rates, covenants and other key terms of our outstanding indebtedness, is included in Part II, Item 8, Note 8, *Debt*, of the Notes to Consolidated Financial Statements included in our Annual Report on Form 10-K for the year ended July 1, 2022. Our delayed draw term loan agreement and the loan agreement governing our revolving credit facility and our Term Loan A-2 due 2027 require us to comply with a leverage ratio financial covenant. As of December 30, 2022, we were in compliance with the applicable financial covenant.

Flash Ventures

Flash Ventures sells to and leases back from a consortium of financial institutions a portion of its tools and has entered into equipment lease agreements of which we guarantee half or all of the outstanding obligations under each lease agreement. The leases are subject to customary covenants and cancellation events that relate to Flash Ventures and each of the guarantors. The occurrence of a cancellation event could result in an acceleration of the lease obligations and a call on our guarantees. As of December 30, 2022, we were in compliance with all covenants under these Japanese lease facilities. See Part I, Item 1, Note 10, *Related Parties and Related Commitments and Contingencies*, of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q for information regarding Flash Ventures.

Purchase Obligations and Other Commitments

In the normal course of business, we enter into purchase orders with suppliers for the purchase of components used to manufacture our products. These purchase orders generally cover forecasted component supplies needed for production during the next quarter, are recorded as a liability upon receipt of the components, and generally may be changed or canceled at any time prior to shipment of the components. We also enter into long-term agreements with suppliers that contain fixed future commitments, which are contingent on certain conditions such as performance, quality and technology of the vendor's components. These arrangements are included under "Purchase obligations and other commitments" in the table above.

Mandatory Deemed Repatriation Tax

The following is a summary of our estimated mandatory deemed repatriation tax obligations that are payable in the following years:

	December 30, 2022
	(in millions)
2024	$ 199
2025	203
2026	255
Total	$ 657

For additional information regarding our estimate of the total tax liability for the mandatory deemed repatriation tax, see Part II, Item 8, Note 13, *Income Tax Expense*, of the Notes to Consolidated Financial Statements included in our Annual Report on Form 10-K for the year ended June 28, 2019.

Unrecognized Tax Benefits

As of December 30, 2022, the liability for unrecognized tax benefits (excluding accrued interest and penalties) was $1.04 billion. Accrued interest and penalties related to unrecognized tax benefits are recognized in liabilities for uncertain tax positions and are recorded in the provision for income taxes. Accrued interest and penalties included in our liability related to unrecognized tax benefits as of December 30, 2022 was $279 million. Of these amounts, approximately $1.18 billion could result in potential cash payments.

As previously disclosed, the IRS issued statutory notices of deficiency and notices of proposed adjustments with respect to transfer pricing with our foreign subsidiaries and intercompany payable balances for years 2008 through 2015. In September 2018 and March 2019, we filed petitions with the U.S. Tax Court covering years 2008 through 2012, for which we had received statutory notices of deficiency, while years 2013 through 2015 remain in the jurisdiction of the IRS's Examination function. The IRS has filed various Amendments to Answer with the U.S. Tax Court which, together with the notices of proposed adjustments, would result in additional federal income tax liabilities totaling approximately $1.6 billion and penalties totaling $449 million with respect to years 2008 through 2015. In May 2022, we and the IRS tentatively reached a settlement for resolving the statutory notices of deficiency and notices of proposed adjustments with respect to years 2008 through 2015 subject to the parties entering into final stipulations and a closing agreement. Based on the tentative settlement for resolution, we now expect to pay tax and interest totaling approximately $720 million to $760 million, which we expect to be partially offset by future reductions to our mandatory deemed repatriation tax obligations and tax savings from interest deductions aggregating to approximately $100 million to $150 million. While we continue to work with the IRS to come to a final agreement on the federal tax and interest calculations, we are uncertain as to when a final agreement will be reached and the exact timing of when any payments will be made. However, we believe it is reasonably likely that these payments may be made within the next twelve months and we have classified that portion of these unrecognized tax benefits, including interest in Income taxes payable on our Condensed Consolidated Balance Sheets as of December 30, 2022. This classification and amount may be subject to change in the next twelve months depending on when we are able to reach a final agreement with the IRS.

Mandatory Research and Development Expense Capitalization

Beginning in 2023, the 2017 Act requires us to capitalize and amortize R&D expenses rather than expensing them in the year incurred, which is expected to result in materially higher cash tax payments in future periods, if not repealed or otherwise modified.

Interest Rate Swap

We have generally held a balance of fixed and variable rate debt and periodically have used interest rate swaps to hedge a portion of our fixed rate debt. As of December 30, 2022, our only variable rate debt outstanding was our Term Loan A-2 on which we had pay-fixed interest rate swaps of $2 billion notional amount that would mitigate the impact of fluctuations in variable interest rates on this loan only through February 2023. See Part I, Item 3, *Quantitative and Qualitative Disclosures About Market Risks* included in this in this Quarterly Report on Form 10-Q for additional information.

Foreign Exchange Contracts

We purchase foreign exchange contracts to hedge the impact of foreign currency fluctuations on certain underlying assets, liabilities and commitments for Operating expenses and product costs denominated in foreign currencies. See Part I, Item 3, *Quantitative and Qualitative Disclosures About Market Risks* included in this Quarterly Report on Form 10-Q for additional information.

Indemnifications

In the ordinary course of business, we may provide indemnifications of varying scope and terms to customers, vendors, lessors, business partners and other parties with respect to certain matters, including, but not limited to, losses arising out of our breach of agreements, products or services to be provided by us, environmental compliance or from intellectual property (“IP”) infringement claims made by third parties. In addition, we have entered into indemnification agreements with our directors and certain of our officers that will require us, among other things, to indemnify them against certain liabilities that may arise by reason of their status or service as directors or officers. We maintain director and officer insurance, which may cover certain liabilities arising from our obligation to indemnify our directors and officers in certain circumstances.

It is not possible to determine the maximum potential amount under these indemnification agreements due to the limited history of prior indemnification claims and the unique facts and circumstances involved in each particular agreement. Such indemnification agreements may not be subject to maximum loss clauses. Historically, we have not incurred material costs as a result of obligations under these agreements.

Stock Repurchase Program

Our Board of Directors has authorized a stock repurchase program for the repurchase of up to $5.0 billion of our common stock, which authorization is effective through July 25, 2023. We did not make any stock repurchases during the six months ended December 30, 2022 and have not repurchased any shares of our common stock pursuant to our stock repurchase program since the first quarter of fiscal 2019. Although we will reevaluate the repurchasing of our common stock when appropriate, there can be no assurance if, when or at what level we may resume such activity. The remaining amount available to be repurchased under our current stock repurchase program as of December 30, 2022 was $4.5 billion. Repurchases under the stock repurchase program may be made in the open market or in privately negotiated transactions and may be made under a Rule 10b5-1 plan.

Recent Accounting Pronouncements

For a description of recently issued and adopted accounting pronouncements, including the respective dates of adoption and expected effects on our results of operations and financial condition, see Part I, Item 1, Note 2, *Recent Accounting Pronouncements*, of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q.

Critical Accounting Policies and Estimates

We have prepared the accompanying unaudited Condensed Consolidated Financial Statements in accordance with accounting principles generally accepted in the United States (U.S. GAAP). The preparation of the financial statements requires the use of judgments and estimates that affect the reported amounts of revenues, expenses, assets, liabilities and shareholders’ equity. We have adopted accounting policies and practices that are generally accepted in the industry in which we operate. If these estimates differ significantly from actual results, the impact to the Condensed Consolidated Financial Statements may be material.

There have been no material changes in our critical accounting policies and estimates from those disclosed in our Annual Report on Form 10-K for the year ended July 1, 2022. Please refer to Part II, Item 7 of our Annual Report on Form 10-K for the year ended July 1, 2022 for a discussion of our critical accounting policies and estimates. In addition, as disclosed in Part I, Item 1, Note 3, *Business Segments, Geographic Information, and Concentrations of Risk*, of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q, as of December 30, 2022, our management identified several factors that warranted a quantitative analysis of impairment for both the Flash and HDD reporting units as of that date. Please refer to that disclosure for additional information on the estimates included in our assessment.

Item 3. *Quantitative and Qualitative Disclosures About Market Risk*

Except as disclosed below, there have been no material changes to our market risk during the six months ended December 30, 2022. See Part II, Item 7A, *Quantitative and Qualitative Disclosures About Market Risks* in our Annual Report on Form 10-K for the year ended July 1, 2022 for further information about our exposure to market risk.

Foreign Currency Risk

Due to macroeconomic changes and volatility experienced in the foreign exchange market recently, we believe sensitivity analysis is more informative in representing the potential impact to the portfolio as a result of market movement. Therefore, we have performed sensitivity analyses as of December 30, 2022 and July 1, 2022 using a modeling technique that measures the change in the fair values arising from a hypothetical 10% adverse movement in the levels of foreign currency exchange rates relative to the U.S. dollar, with all other variables held constant. The analyses cover all of our foreign currency derivative contracts used to offset the underlying exposures. The foreign currency exchange rates used in performing the sensitivity analyses were based on market rates in effect at December 30, 2022 and July 1, 2022. The sensitivity analyses indicated that a hypothetical 10% adverse movement in foreign currency exchange rates relative to the U.S. dollar would result in a foreign exchange fair value loss of $342 million and $306 million at December 30, 2022 and July 1, 2022, respectively.

Interest Rate Risk

We have generally held a balance of fixed and variable rate debt. As of December 30, 2022, our only variable rate debt outstanding was our Term Loan A-2, which bears interest, at the Company's option, at a per annum rate equal to either (x) the Adjusted Term Secured Overnight Financing Rate ("SOFR") (as defined in the Loan Agreement) plus an applicable margin varying from 1.125% to 2.000% or (y) a base rate plus an applicable margin varying from 0.125% to 1.000%, in each case depending on the corporate family ratings of the Company from at least two of Standard & Poor's Ratings Services, Moody's Investors Service, Inc. and Fitch Ratings, Inc., with an initial interest rate of Adjusted Term SOFR plus 1.375%.

As of December 30, 2022, the outstanding balance on our Term Loan A-2 was $2.7 billion and a one percent increase in the variable rate of interest would increase annual interest expense by $27 million. We currently have pay-fixed interest rate swaps of $2 billion notional amount that would mitigate the impact of fluctuations in variable interest rates only through February 2023.

Item 4. *Controls and Procedures*

Evaluation of Disclosure Controls and Procedures

As required by Rule 13a-15(b) promulgated by the Securities and Exchange Commission under the Securities Exchange Act of 1934, as amended (the "Exchange Act"), we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as such term is defined in Rule 13a-15(e) under the Exchange Act) as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this Quarterly Report on Form 10-Q, our disclosure controls and procedures were effective.

Changes in Internal Controls over Financial Reporting

There has been no change in our internal control over financial reporting during the second quarter of 2023 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

PART II. OTHER INFORMATION

Item 1. *Legal Proceedings*

See Note 13, *Income Tax Expense*, of the Notes to Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q for disclosures regarding statutory notices of deficiency issued by the IRS in June 2018 and December 2018, petitions filed by the Company with the U.S. Tax Court in September 2018 and March 2019, additional penalties asserted by the IRS in March 2021 and further Amendments to Answers filed by the IRS in June 2021 and January 2022, and a tentative resolution with respect to certain matters.

Item 1A. *Risk Factors*

We have described under the heading “Risk Factors” in Part I, Item 1A of our Annual Report on Form 10-K for the year ended July 1, 2022 risks and uncertainties that could cause our actual results of operations and financial condition to vary materially from past, or from anticipated future, results of operations and financial condition. There have been no material changes from these risk factors previously described in our Annual Report on Form 10-K for the year ended July 1, 2022. These risks and uncertainties are not the only risks facing us. Additional risks and uncertainties not presently known to us or that we currently deem immaterial may also adversely affect our business, financial condition, results of operations or the market price of our common stock.

Item 6. ***Exhibits***

The exhibits listed in the Exhibit Index below are filed with, or incorporated by reference in, this Quarterly Report on Form 10-Q, as specified in the Exhibit List, from exhibits previously filed with the Securities and Exchange Commission. Certain agreements listed in the Exhibit Index that we have filed or incorporated by reference may contain representations and warranties by us or our subsidiaries. These representations and warranties have been made solely for the benefit of the other party or parties to such agreements and (i) may have been qualified by disclosures made to such other party or parties, (ii) were made only as of the date of such agreements or such other date(s) as may be specified in such agreements and are subject to more recent developments, which may not be fully reflected in our public disclosures, (iii) may reflect the allocation of risk among the parties to such agreements and (iv) may apply materiality standards different from what may be viewed as material to investors. Accordingly, these representations and warranties may not describe the actual state of affairs at the date hereof and should not be relied upon.

EXHIBIT INDEX

Exhibit Number	Description
3.1	Amended and Restated Certificate of Incorporation of Western Digital Corporation, as amended to date (Filed as Exhibit 3.1 to the Company's Quarterly Report on Form 10-Q (File No. 1-08703) with the Securities and Exchange Commission on February 8, 2006)
3.2	Amended and Restated By-Laws of Western Digital Corporation, as amended effective as of February 10, 2021 (Filed as Exhibit 3.1 to the Company's Current Report on Form 8-K (File No. 1-08703) with the Securities and Exchange Commission on February 12, 2021)
10.1	Western Digital Corporation Amended and Restated 2021 Long-Term Incentive Plan, amended and restated as of August 25, 2022 (Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K (File No. 1-08703) with the Securities and Exchange Commission on November 18, 2022)*
10.2	Western Digital Corporation Amended and Restated 2005 Employee Stock Purchase Plan, amended and restated as of August 25, 2022 (Filed as Exhibit 10.2 to the Company's Current Report on Form 8-K (File No. 1-08703) with the Securities and Exchange Commission on November 18, 2022)*
10.3	Amendment No. 1, dated as of December 23, 2022, to the Amended and Restated Loan Agreement, dated as of January 7, 2022, by and among Western Digital Corporation, each lender party thereto, J.P. Morgan Chase Bank, N.A. as Administrative Agent and the other parties thereto (Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K (File No. 1-08703) with the Securities and Exchange Commission on December 23, 2022)
10.4	Loan Agreement, dated as of January 25, 2023, by and among Western Digital Corporation, each lender party thereto, J.P. Morgan Chase Bank, N.A. as administrative agent and the other parties thereto (Filed as Exhibit 10.1 to the Company's Current Report on Form 8-K (File No.1-08703) with the Securities and Exchange Commission on January 31, 2023)
31.1	Certification of Principal Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002†
31.2	Certification of Principal Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002†
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**
32.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002**
101.INS	XBRL Instance Document - the instance document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document
101.SCH	XBRL Taxonomy Extension Schema Document†
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document†
101.LAB	XBRL Taxonomy Extension Label Linkbase Document†
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document†
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document†
104	Cover Page Interactive Data File - formatted in Inline XBRL and contained in Exhibit 101

† Filed with this report.

* Management contract or compensatory plan or arrangement required to be filed as an exhibit pursuant to applicable rules of the Securities and Exchange Commission.

** Furnished with this report.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this Quarterly Report on Form 10-Q to be signed on its behalf by the undersigned thereunto duly authorized.

WESTERN DIGITAL CORPORATION

By: /s/ Gene Zamiska

Gene Zamiska

Senior Vice President, Global Accounting and Chief Accounting Officer

(Principal Accounting Officer)

Dated: February 2, 2023

Exhibit 31.1

CERTIFICATION OF PRINCIPAL EXECUTIVE OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, David V. Goeckeler, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Western Digital Corporation;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15(d)-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ David V. Goeckeler
David V. Goeckeler
Chief Executive Officer

Dated: February 2, 2023

Exhibit 31.2

CERTIFICATION OF PRINCIPAL FINANCIAL OFFICER
PURSUANT TO SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002

I, Wissam Jabre, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Western Digital Corporation;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15(d)-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

/s/ Wissam Jabre

Wissam Jabre
Executive Vice President and Chief Financial Officer
(Principal Financial Officer)

Dated: February 2, 2023

Exhibit 32.1

The following certification is being furnished solely to accompany the Report pursuant to 18 U.S.C. § 1350 and in accordance with SEC Release No. 33-8238. This certification shall not be deemed “filed” for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liability of that section, nor shall it be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, except to the extent that Western Digital Corporation specifically incorporates it by reference.

Certification of Chief Executive Officer

Pursuant to 18 U.S.C. § 1350, as created by Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned officer of Western Digital Corporation, a Delaware corporation (the “Company”), hereby certifies, to his knowledge, that:

(i) the accompanying Quarterly Report on Form 10-Q of the Company for the period ended December 30, 2022 (the “Report”) fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934, as amended; and

(ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ David V. Goeckeler

David V. Goeckeler
Chief Executive Officer

Dated: February 2, 2023

Exhibit 32.2

The following certification is being furnished solely to accompany the Report pursuant to 18 U.S.C. § 1350 and in accordance with SEC Release No. 33-8238. This certification shall not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, as amended, or otherwise subject to the liability of that section, nor shall it be incorporated by reference into any filing of the Company under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, except to the extent that Western Digital Corporation specifically incorporates it by reference.

Certification of Chief Financial Officer

Pursuant to 18 U.S.C. § 1350, as created by Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned officer of Western Digital Corporation, a Delaware corporation (the "Company"), hereby certifies, to his knowledge, that:

(i) the accompanying Quarterly Report on Form 10-Q of the Company for the period ended December 30, 2022 (the "Report") fully complies with the requirements of Section 13(a) or Section 15(d), as applicable, of the Securities Exchange Act of 1934, as amended; and

(ii) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Wissam Jabre

Wissam Jabre
Executive Vice President and Chief Financial Officer
(Principal Financial Officer)

Dated: February 2, 2023