

IEC ELECTRONICS CORP

Form 10-K

December 06, 2017

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

Annual Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the fiscal year ended September 30, 2017

or

Transition Report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 001-34376

IEC ELECTRONICS CORP.

(Exact name of registrant as specified in its charter)

Delaware

13-3458955

(State or other jurisdiction of incorporation or organization) (IRS Employer Identification No.)

105 Norton Street, Newark, New York 14513

(Address of principal executive offices) (Zip code)

Registrant's telephone number, including area code: 315-331-7742

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

Common Stock, \$.01 par value NYSE AMERICAN LLC

(Title of each class) (Name of each exchange on which registered)

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes  No

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 and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. x

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. (Check one):

Large accelerated filer " Accelerated filer "

Non-accelerated filer " Smaller reporting company x

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 x

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At March 31, 2017, the last business day of the registrant's second quarter for the fiscal year ended September 30, 2017, the aggregate market value of the shares of common stock held by non-affiliates of the registrant was \$34,410,666 (based on the closing price of the registrant's common stock on the NYSE American on such date). Shares of common stock held by each executive officer and director and by each person and entity who beneficially owns more than 10% of the outstanding common stock have been excluded in that such person or entity may be deemed to be an affiliate for purposes of this calculation. Such exclusion should not be deemed a determination or admission by registrant that such individuals or entities are, in fact, affiliates of the registrant. As of December 1, 2017, there were 10,325,507 shares of common stock outstanding.

**DOCUMENTS INCORPORATED BY REFERENCE**

Portions of IEC Electronics Corp.'s definitive Proxy Statement to be filed with the Securities and Exchange Commission in connection with its 2018 Annual Meeting of Stockholders are incorporated by reference into Part III Items 10, 11, 12, 13 and 14 of this Form 10-K.

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## CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

References in this report to “IEC,” the “Company,” “we,” “our,” or “us” mean IEC Electronics Corp. and its subsidiaries except where the context otherwise requires. This Annual Report on Form 10-K for the fiscal year ended September 30, 2017 (“Form 10-K”) contains forward-looking statements. In some cases you can identify forward-looking statements by terms such as “may,” “will,” “should,” “expects,” “plans,” “anticipates,” “could,” “intends,” “targets,” “projects,” “contemplates,” “believes,” “estimates,” “predicts,” “potential” or “continue” or the negative of these terms or other similar expressions. These forward-looking statements include, but are not limited to, statements regarding future sales and operating results, future prospects, the capabilities and capacities of business operations, any financial or other guidance and all statements that are not based on historical fact, but rather reflect our current expectations concerning future results and events. The ultimate correctness of these forward-looking statements is dependent upon a number of known and unknown risks and events and is subject to various uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by these forward-looking statements.

The following important factors, among others, could affect future results and events, causing those results and events to differ materially from those views expressed or implied in our forward-looking statements: business conditions and growth or contraction in our customers’ industries, the electronic manufacturing services industry and the general economy; variability of our operating results; our ability to control our material, labor and other costs; our dependence on a limited number of major customers; the potential consolidation of our customer base; availability of component supplies; dependence on certain industries; variability and timing of customer requirements; technological, engineering and other start-up issues related to new programs and products; uncertainties as to availability and timing of governmental funding for our customers; the impact of government regulations, including FDA regulations; the types and mix of sales to our customers; litigation and governmental investigations or proceedings arising out of or relating to accounting and financial reporting matters; intellectual property litigation; our ability to maintain effective internal controls over financial reporting; unforeseen product failures and the potential product liability claims that may be associated with such failures; the availability of capital and other economic, business and competitive factors affecting our customers, our industry and business generally; failure or breach of our information technology systems; and natural disasters. Any one or more of such risks and uncertainties could have a material adverse effect on us or the value of our common stock. For a further list and description of various risks, relevant factors and uncertainties that could cause future results or events to differ materially from those expressed or implied in our forward-looking statements, see the “Risk Factors” and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” sections elsewhere in this Form 10-K and other filings with the Securities and Exchange Commission (the “SEC”).

All forward-looking statements included in this Form-10-K are made only as of the date indicated or as of the date of this Form 10-K. We do not undertake any obligation to, and may not, publicly update or correct any forward-looking statements to reflect events or circumstances that subsequently occur or which we hereafter become aware of, except as required by law. New risks and uncertainties arise from time to time and we cannot predict these events or how they may affect us and cause actual results to differ materially from those expressed or implied by our forward-looking statements. Therefore, you should not rely on our forward-looking statements as predictions of future events. When considering these risks, uncertainties and assumptions, you should keep in mind the cautionary statements contained in this report and any documents incorporated herein by reference. You should read this document and the documents that we reference in this Form-10-K completely and with the understanding that our actual future results may be materially different from what we expect. All forward-looking statements attributable to us are expressly qualified by these cautionary statements.



## PART I

### Item 1. BUSINESS

#### Overview

IEC Electronics Corp. (“IEC,” “we,” “our,” “us,” “Company”) conducts business directly, as well as through its subsidiaries, IEC Electronics Wire and Cable, Inc (“Wire and Cable”) that merged into IEC on December 28, 2016, IEC Electronics Corp-Albuquerque (“Albuquerque”), IEC Analysis & Testing Laboratory, LLC (“ATL”) and IEC California Holdings, Inc. The Rochester unit, formerly known as Celmet, operates as a division of IEC.

We are a premier provider of electronic manufacturing services (“EMS”) to advanced technology companies that produce life-saving and mission critical products for the medical, industrial, aerospace and defense sectors. We specialize in delivering technical solutions for the custom manufacturing, product configuration, and verification testing of highly engineered complex products that require a sophisticated level of manufacturing to ensure quality and performance.

Within the EMS sector, we have unique capabilities which allow our customers to rely on us to solve their complex challenges, minimize their supply chain risk and deliver full system solutions for their supply chain. These capabilities include, among others:

Our engineering services include the design, development, and fabrication of customized stress testing platforms to simulate a product’s end application, such as thermal cycling and vibration, in order to ensure reliable performance and avoid catastrophic failure when the product is placed in service.

Our vertical manufacturing model offers customers the ability to simplify their supply chain by utilizing a single supplier for their critical components including complex printed circuit board assembly (“PCBA”), precision metalworking, and interconnect solutions. This service model allows us to control the cost, lead time, and quality of these critical components which are then integrated into full system assemblies and minimizes our customers’ supply chain risk.

We provide direct order fulfillment services for our customers by integrating with their configuration management process to obtain their customer orders, customize the product to the specific requirements, functionally test the product and provide verification data, and direct ship to their end customer in order to reduce time, cost, and complexity within our customer's supply chain.

We are the only EMS provider with an on-site laboratory that has been approved by the Defense Logistics Agency (“DLA”) for their Qualified Testing Supplier List (“QTSL”) program which deems the site suitable to conduct various QTSL and military testing standards including counterfeit component analysis. In addition, this advanced laboratory is utilized for complex design analysis and manufacturing process development to solve challenges and accelerate our customers’ time to market.

We are a 100% US manufacturer which attracts customers who are unlikely to utilize offshore suppliers due to the proprietary nature of their products, governmental restrictions or volume considerations. Our locations include:

Newark, New York - Located approximately one hour east of Rochester, NY, our Newark location is our corporate headquarters and is the largest manufacturing location providing complex circuit board manufacturing, interconnect solutions, and system-level assemblies along with an on-site material analysis laboratory for advanced manufacturing process development.

Rochester, New York - Focuses on precision metalworking services including complex metal chassis and assemblies.

Albuquerque, New Mexico - Specializes in the aerospace and defense markets with complex circuit board and system-level assemblies along with a state of the art analysis and testing laboratory which conducts counterfeit component analysis and complex design analysis.

We excel at complex, highly engineered products that require sophisticated manufacturing support where quality and reliability are of paramount importance. With our customers at the center of everything we do, we have created a high-intensity, rapid response culture capable of reacting and adapting to their ever-changing needs. Our customer-centric approach offers a high degree of flexibility while simultaneously complying with rigorous quality and on-time delivery standards.

We proactively invest in areas we view as important for our continued long-term growth. All of our locations are ISO 9001:2008 certified and ITAR registered. We are Nadcap accredited and AS9100C certified at our Newark and Albuquerque locations to support the stringent quality requirements of the aerospace industry. Our Newark location is ISO 13485 certified to serve the medical market sector and is an approved supplier by the National Security Agency (“NSA”) under the COMSEC standard regarding communications security. Our analysis & testing laboratory in Albuquerque is ISO 17025 accredited, an IPC-approved Validation Services test Laboratory, and is the only on-site EMS laboratory that has been approved by the DLA



for their QTSL program which deems the site suitable to conduct various QTSL and military testing standards including counterfeit component analysis. Albuquerque also performs work per NASA-STD-8739 and J-STD-001ES space standards.

The technical expertise of our experienced workforce enables us to build some of the most advanced electronic, wire and cable, interconnect solutions, and precision metal systems sought by original equipment manufacturers (“OEMs”).

#### Organization

IEC Electronics Corp., a Delaware corporation, is the successor by merger in 1990 to IEC Electronics Corp., a New York corporation, which was originally organized in 1966. Our executive offices are located at 105 Norton Street, Newark, New York 14513. Our telephone number is 315-331-7742, and our Internet address is [www.iec-electronics.com](http://www.iec-electronics.com).

We have executed several strategic acquisitions over the past decade to advance our capability to support existing and potential customers in the EMS market.

On December 17, 2010, we acquired the assets of Southern California Braiding Co., Inc., a privately held company principally engaged in providing wire and cable products to aerospace and defense markets. The business was operated through IEC’s subsidiary, Southern California Braiding, Inc. (“SCB”). SCB was divested during the fourth quarter of 2015.

#### The Electronics Contract Manufacturing Services Industry

The EMS industry specializes in providing the program management, technical support and manufacturing expertise required to take a product from the early design and prototype stages through volume production and distribution. Primarily as a response to rapid technological change and increased competition in the electronics industry, OEMs have recognized that by utilizing EMS providers they can improve their competitive position, realize an improved return on investment and concentrate on their core competencies such as research, product design and development and marketing. In addition, EMS providers allow OEMs to bring new products to market more rapidly and to adjust more quickly to fluctuations in product demand; avoid additional investment in plant, equipment and personnel; reduce inventory and other overhead costs; and determine known unit costs over the life of a contract. Many OEMs now consider EMS providers valued partners in executing their business and manufacturing strategy.

OEMs increasingly require EMS providers to provide complete turn-key manufacturing and material handling services rather than working on a consignment basis in which the OEM supplies all materials and the EMS provider supplies labor. Turn-key contracts involve design, manufacturing and engineering support, the procurement of all materials, sophisticated in-circuit and functional testing, and distribution.

#### IEC’s Strategy

IEC is focused on providing services for life-saving and mission critical products in the medical, industrial, aerospace and defense sectors that require a sophisticated level of manufacturing support. We offer our customers a full range of manufacturing services, combined with advanced scientific technical support to ensure their products perform for the critical applications for which they are intended. The ability to solve our customers' technical challenges, meet their stringent quality requirements, and integrate seamlessly within their supply chain, is the value add that IEC brings.

We often engage with our customers in the early stages of product or program design, work with customers to evaluate the manufacturability and testability of their products, with the objective of enhancing quality and reducing

the overall cost of ownership for our customers. Due to the highly regulated environment for many of our customers, they are seeking a long term partnership throughout the life-cycle of their product.

We are a certified small business with advanced technical capabilities. This allows us to focus on our customer's needs and deliver solutions in a responsive manner to accelerate their time to market.

### Competition

The EMS industry is highly fragmented and characterized by intense competition. We believe that the principal competitive factors in the EMS market include: technology capabilities, quality and range of services, past performance, design, cost, responsiveness and flexibility. We specialize in the custom manufacture of life-saving and mission critical products that require complex circuit boards and system-level assemblies; a wide array of cable and wire harness assemblies capable of withstanding extreme environments; and precision metal components.

We are certified to serve the military and commercial aerospace sector as well as the medical sector and we hold various accreditations. We believe we excel where quality and reliability are of paramount importance and when low-to-medium volume, high-mix production is the norm. We utilize state-of-the-art, automated circuit board assembly equipment together with a full complement of high-reliability manufacturing stress testing methods. Our customer-centric approach offers a high degree of flexibility while simultaneously complying with rigorous quality and on-time delivery standards.

We compete against numerous foreign and domestic companies in addition to the internal capabilities of some of our customers. Some of our competitors include Sparton Corporation, Benchmark Electronics, Inc., Plexus Corp. and Ducommun Incorporated. We may face new competitors in the future as the outsourcing industry evolves and existing or start-up companies develop capabilities similar to ours.

#### Products and Services

We manufacture a wide range of assemblies that are incorporated into many different products, such as aerospace and defense systems, medical devices, industrial equipment and transportation products. Our products are distributed to and through OEMs. We support multiple divisions and product lines for many of our customers and frequently manufacture successive generations of products. In some cases, we are the sole EMS contract manufacturer for the customer site or division.

#### Materials Management

We generally procure materials to meet specific contract requirements and are often protected by contract terms that call for reimbursement to us in the event a contract is terminated by the customer. Whether purchased by us or supplied by a customer, materials are tracked and controlled by our internal systems throughout the manufacturing process.

#### Availability of Components

Our revenues are principally derived from turn-key services that involve the acquisition of raw and component materials, often from a limited number of suppliers, to be manufactured in accordance with each customer's specifications. While we believe we are well positioned with supplier relationships and procurement expertise, potential shortages of components in the world market could materially adversely affect our revenue levels or operating efficiencies.

#### Suppliers

Although we depend on a limited number of key suppliers, as a result of strategic relationships we have established with them, the Company frequently benefits from one or more of the following enhancements: reduced lead-times; competitive pricing; favorable payment terms; and preference during periods of limited supply. We have preferred supplier partnership agreements in place to support our business generally and to ensure access to custom commodities, such as printed circuit boards.

For the year ended September 30, 2017 ("fiscal 2017"), IEC obtained 30% of the materials used in production from two vendors, Avnet, Inc. and Arrow Electronics, Inc. If either of these vendors were to cease supplying us with materials for any reason, we would be forced to find alternative sources of supply. A change in suppliers could cause a delay in availability of products and a possible loss of sales, which could adversely affect operating results.

#### Marketing and Sales

We utilize a direct sales force as well as a nationwide network of manufacturer's representatives. Through this hybrid sales approach, we execute a focused sales strategy targeting those customers whose product profiles are aligned with our core areas of expertise. For example, we focus on customers that are developing complex, advanced technology products for a wide array of market sectors ranging from satellite communications to medical, military and ruggedized industrial products.

Typically, the demand profiles associated with these customers are in the low-to-moderate volume range with high variability in required quantities and product mix. These customers' products often employ emerging technologies that require concentrated engineering and manufacturing support from product development through prototyping and on to volume manufacturing, which can result in significant lead times before full production and are difficult to forecast. As a result of the specialized services required, such customers rarely rely on an outsourcing model that focuses primarily on minimizing costs.

To reduce risk, the Company seeks a balanced distribution of business across industry sectors. As indicated in the table that follows, this can fluctuate based on end customer demands.

% of Sales by Sector	Years Ended	
	September 30, 2017	September 30, 2016
Aerospace and Defense	52%	40%
Medical	28%	42%
Industrial	18%	16%
Other	2%	2%
	100%	100%

Individual customers representing 10% or more of sales in fiscal 2017 included Baxter Corporation (“Baxter”) (14%), in the medical sector, and ViaSat Inc. (13%), in the aerospace and defense sector, and in fiscal 2016, Zoll Lifecor Corporation (15%), and Baxter (15%), both of which are in the medical sector.

Three customers represented 10% or more of receivables at September 30, 2017. Two customers in the aerospace and defense sector and one customer in the medical sector together accounted for 42% of the outstanding balances at September 30, 2017. Three customers represented 10% or more of receivables at September 30, 2016. One customer each in the medical, aerospace and defense, and industrial sectors together accounted for 40% of the outstanding balances at September 30, 2016.

#### Backlog

Our backlog at the end of fiscal 2017 was \$72.1 million, which is 33.3% higher than \$54.1 million at the end of fiscal 2016. Backlog consists of two categories: purchase orders and firm forecasted commitments. In addition to fulfilling orders and commitments contained in quarter-end backlog reports, we also receive and ship orders within each quarter that do not appear in the period end backlog reports. Variations in the magnitude and duration of contracts as well as customer delivery requirements may result in fluctuations in backlog from period to period. Approximately \$66.3 million of our backlog at September 30, 2017 is expected to be shipped within the fiscal year ending September 30, 2018 (“fiscal 2018”), with the remainder expected to ship in future years. This compares to \$46.3 million that was expected to be shipped within 12 months from year-end as of September 30, 2016, with the remainder at such time that was expected to be shipped greater than 12 months from the prior year-end.

#### Governmental Regulation

Our operations are subject to certain United States government regulations that control the export and import of defense-related articles and services, as well as federal, state and local regulatory requirements relating to environmental protection, waste management, and employee health and safety matters. We believe that our business is operated in substantial compliance with all applicable laws and governmental regulations. While current costs of compliance, including compliance with environmental laws, are not material, our expenses could increase if new laws, regulations or requirements were to be introduced. Some of our medical and other customers are highly regulated. Any failure to comply by customers, related to products we produce for them, can delay or disrupt their orders from us.

#### Employees

Employees are our single greatest resource. IEC’s total employees numbered 565, all of which are full time employees, at September 30, 2017. The Company decreased by 69 employees during fiscal 2017, mainly driven by lower volumes in fiscal 2017. Some of our full-time employees are temporary employees. We make a concerted effort to engage our

employees in initiatives that improve our business and provide opportunities for growth, and we believe that our employee relations are good. We have access to large and technically qualified workforces in close proximity to our operating locations in Rochester, NY and Albuquerque, NM.

#### Sale-Leaseback Transaction

On November 18, 2016, we completed a sale-leaseback transaction pursuant to which our subsidiary, Albuquerque, sold certain property, including its manufacturing facility located in Albuquerque, New Mexico, to Store Capital Acquisitions, LLC for an aggregate purchase price of approximately \$5.8 million including a \$120.0 thousand holdback. Proceeds from this transaction were used to pay the mortgage on such property and pay down Term Loan A, as discussed in Note 5—Credit Facilities. As part of the transaction, Albuquerque entered into a lease for the property for an initial term of 15 years that may be renewed twice for five-year terms. The initial base annual rental is approximately \$474.0 thousand and is subject to certain annual increases. In addition, we entered into a separate payment and performance guaranty with Store Capital Acquisitions, LLC with respect to the lease. The sale-leaseback transaction is further described in Note 12—Capital Lease.

#### Patents and Trademarks

We hold one patent and have two patent applications pending related to counterfeit detection. We employ various registered trademarks. We do not believe that either patent or trademark protection is material to the operation of our business.

## Item 1A. RISK FACTORS

We depend on a relatively small number of customers, the loss of one or more of whom may negatively affect our operating results.

A relatively small number of customers are responsible for a significant portion of our net sales. During fiscal 2017 and 2016, our five largest customers accounted for 49% and 53% of net sales, respectively. During fiscal 2017, we saw a significant reduction in sales to two large customers. The percentage of our sales to our major customers may fluctuate from period to period, and our principal customers may also vary from year to year. Significant reduction in sales to any of our major customers, or the loss of a major customer, could have a material adverse effect on our results of operations and financial condition.

We rely on the continued growth and financial stability of our customers, including our major customers. Adverse changes in the end markets they serve can reduce demand from our customers in those markets and/or make customers in these end markets more price sensitive. Further, mergers or restructurings among our customers, or their end customers, could increase concentration or reduce total demand as the combined entities reevaluate their business and consolidate their suppliers. Future developments, particularly in those end markets that account for more significant portions of our revenues, could harm our business and our results of operations.

Because of this concentration in our customer base, we have significant amounts of trade accounts receivable from some of our customers. If one or more of our customers experiences financial difficulty and is unable to provide timely payment for the services provided, our operating results and financial condition could be adversely affected.

In addition, consolidation among our customers could intensify this concentration and adversely affect our business. In the event of consolidation among our customers, depending on which organization controls the supply chain function following the consolidation, we may not be retained as a preferred or approved supplier. In addition, product duplication could result in the termination of a product line that we currently support. While there is potential for increasing our position with the combined customer, our revenues could decrease if we are not retained as a continuing supplier. Even if we are retained as a supplier, we may also face the risk of increased pricing pressure from the combined customer because of its increased market share.

Our operating results may fluctuate from period to period.

Our annual and quarterly operating results may fluctuate significantly depending on various factors, many of which are beyond our control. These factors may include, but are not necessarily limited to:

- adverse changes in general economic conditions;
- natural disasters that may impede our operations, the operation of our customers' business, or availability of manufacturing inputs from our suppliers;
- the level and timing of customer orders and the accuracy of customer forecasts;
- the capacity utilization of our manufacturing facilities and associated fixed costs;
- price competition;
- market acceptance of our customers' products;
- business conditions in our customers' end markets;
- our level of experience in manufacturing a particular product;
- changes in the mix of sales to our customers;
- variations in efficiencies achieved in managing inventories and property, plant and equipment;
- fluctuations in cost and availability of materials;



• timing of expenditures in anticipation of future orders;  
• changes in cost and availability of labor and components;  
• our effectiveness in managing the high reliability manufacturing process required by our customers; and  
• failure or external breach of our information technology systems.

The EMS industry is affected by the United States and global economies, both of which are influenced by world events. An economic slowdown, particularly in the industries we serve, may result in our customers reducing their forecasts or delaying orders. The demand for our services could weaken, which in turn could substantially influence our sales, capacity utilization, margins and financial results. Recent periods in which EMS sales were adversely affected include Department of Defense spending reductions resulting from sequestration and a partial government shut-down during 2013.

The agreements governing our debt contain various covenants that may constrain the operation of our business, and our failure to comply with these covenants may have a material adverse effect on our financial condition.

The agreements and instruments governing our secured bank credit facility (the “Credit Facility”) with Manufacturers and Traders Trust Company (“M&T Bank”) and other existing debt contain various covenants that, among other things, require us to comply with certain financial covenants including maintenance of a fixed charge coverage ratio (“Financial Covenants”). The agreements and instruments governing the Credit Facility require financial and other reporting, contain limitations on revolving loan borrowings and restrict or limit our ability to:

- incur debt;
- incur or maintain liens;
- make acquisitions of businesses or entities;
- make investments, loans or advances;
- enter into guarantee agreements;
- engage in mergers, consolidations or certain sales of assets;
- engage in transactions with affiliates;
- pay dividends at the parent level, or engage in stock redemptions or repurchases; and
- make capital expenditures.

The Credit Facility is secured by a general security agreement covering the assets of the Company and its subsidiaries, a pledge of the Company’s equity interest in its subsidiaries, a negative pledge on the Company’s real property, and a guarantee by the Company’s subsidiaries, all of which restrict use of these assets to support other financial instruments.

To the extent we are required to seek additional waivers and/or amendments, we may continue to experience increased borrowing costs. If the Company is not in compliance with all of our debt covenants, and if M&T Bank chooses to exercise its remedies, M&T Bank could accelerate our primary indebtedness which could cause cross-defaults with respect to other obligations, causing a material adverse effect on our financial condition including, our inability to obtain replacement financing or continue operations. Our ability to comply with covenants contained in our Credit Facility and other existing debt may be affected by events beyond our control, including prevailing economic, financial and industry conditions.

We participate in the electronics industry, which historically produces technologically advanced products with short life cycles.

Factors affecting the electronics industry in general could seriously harm our customers and, as a result, us. These factors may include, but may not be limited to:

- the inability of our customers to adapt to rapidly changing technology and evolving industry standards, which result in short product life cycles;
- the inability of our customers to develop and market their products, some of which are new and untested;
  - increased competition among our customers and their competitors, including downward pressure on pricing;
- the potential that our customers’ products may become obsolete, or the failure of our customers’ products to gain anticipated commercial acceptance; and
- periods of significantly decreased demand in our customers’ markets.

Since a significant portion of our business is defense-related, reductions or delays in U.S. defense spending may materially adversely affect our revenues.

During fiscal years 2017 and 2016, our sales to customers serving the aerospace and defense industries approximated 52% and 40% of our sales, respectively. Because these products and services are ultimately sold to the U.S. government by our customers, these sales are affected by, among other things, the federal budget process, which is driven by numerous factors beyond our control, including geo-political, macroeconomic and political conditions. The contracts between our direct customers and their government customers are subject to political and budgetary constraints and processes, changes in short-range and long-range strategic plans, the timing of contract awards, the congressional budget authorization and appropriation processes, the government's ability to terminate contracts for convenience or for default, as well as other risks such as contractor suspension or debarment in the event of certain violations of legal and regulatory requirements.

While we believe that our customers' programs are well aligned with national defense and other priorities, shifts in domestic and international spending and tax policy, changes in security, defense and intelligence priorities, the affordability of our products and services, general economic conditions and developments, and other factors may affect a decision to fund or the level of funding for existing or proposed programs. An impasse in federal budget decision-making could lead to substantial delays or reductions in federal spending. For example, as a result of the inability of the U.S. Government to reach agreement

on budget reduction measures required by the Budget Control Act of 2011, sequestration triggered very substantial automatic spending reductions beginning in January 2013, divided between defense and domestic spending over a nine-year period. As a result, U.S. Government funding for certain of our customers has been and could continue to be reduced, delayed or eliminated, which could significantly impact these customers' demand for our products and services and if so this could have a material adverse effect on our business, results of operations and cash flows.