

METHODE ELECTRONICS INC

Form 10-Q

December 06, 2018

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

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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 October 27, 2018

or

Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the transition period from \_\_\_\_\_ to \_\_\_\_\_

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Commission file number 0-2816

METHODE ELECTRONICS, INC.

(Exact name of registrant as specified in its charter)

Delaware 36-2090085  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)

8750 West Bryn Mawr Avenue, Suite 1000, Chicago, Illinois 60631-3518  
(Address of principal executive offices) (Zip Code)

(Registrant's telephone number, including area code) (708) 867-6777

7401 West Wilson Avenue, Chicago, Illinois 60706  
(Former name, former address and former fiscal year, if changed since last report)

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 during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes  No

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

Large accelerated filer  Accelerated filer   
Non-accelerated filer  Smaller reporting company

Emerging Growth Company o

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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 Securities Act.

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

At December 4, 2018, registrant had 36,986,952 shares of common stock outstanding.

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## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

METHODE ELECTRONICS, INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF INCOME (Unaudited)

(Dollars in millions, except per share data)

|   | Three Months Ended |              | Six Months Ended |              |
|---|--------------------|--------------|------------------|--------------|
|   | October 2018       | October 2017 | October 2018     | October 2017 |
| Net Sales   | \$264.0            | \$ 230.1     | \$487.4          | \$ 431.3     |
| Cost of Products Sold                                 | 193.2              | 168.1        | 356.5            | 313.7        |
| Gross Profit  | 70.8               | 62.0         | 130.9            | 117.6        |
| Selling and Administrative Expenses                   | 48.0               | 31.2         | 77.5             | 60.8         |
| Amortization of Intangibles                           | 3.7                | 1.1          | 5.6              | 1.7          |
| Income from Operations                                | 19.1               | 29.7         | 47.8             | 55.1         |
| Interest Expense, Net                                 | 1.6                | 0.2          | 1.8              | —            |
| Other Expense (Income), Net                           | (0.1)              | 0.4          | 0.2              | 1.2          |
| Income before Income Taxes                            | 17.6               | 29.1         | 45.8             | 53.9         |
| Income Tax Expense                                    | 3.0                | 4.9          | 7.5              | 9.2          |
| Net Income  | \$14.6             | \$ 24.2      | \$38.3           | \$ 44.7      |
| Basic and Diluted Income per Share:                   |                    |              |                  |              |
| Basic   | \$0.39             | \$ 0.65      | \$1.02           | \$ 1.20      |
| Diluted   | \$0.39             | \$ 0.64      | \$1.02           | \$ 1.19      |
| Cash Dividends:                                       |                    |              |                  |              |
| Common Stock  | \$0.11             | \$ 0.09      | \$0.22           | \$ 0.18      |
| Weighted Average Number of Common Shares Outstanding: |                    |              |                  |              |
| Basic   | 37,405,550         | 37,283,500   | 37,377,997       | 37,266,095   |
| Diluted   | 37,673,727         | 37,668,100   | 37,648,048       | 37,629,640   |

See notes to condensed consolidated financial statements.

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METHODE ELECTRONICS, INC. AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (Unaudited)  
 (Dollars in millions)

|   | Three Months Ended |                  | Six Months Ended |                  |
|---|--------------------|------------------|------------------|------------------|
|   | October 27, 2018   | October 28, 2017 | October 27, 2018 | October 28, 2017 |
| Net Income                              | \$14.6             | \$ 24.2          | \$38.3           | \$ 44.7          |
| Foreign Currency Translation Adjustment | (7.7 )             | (6.5 )           | (25.6 )          | 18.1             |
| Comprehensive Income                    | \$6.9              | \$ 17.7          | \$12.7           | \$ 62.8          |

See notes to consolidated financial statements.

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METHODE ELECTRONICS, INC. AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 (Dollars in millions, except per share amounts)

|   | October 27,<br>2018 | April 28,<br>2018 |
|---|---------------------|-------------------|
|   | (Unaudited)         |                   |
| Assets:                                   |                     |                   |
| Current Assets:                           |                     |                   |
| Cash and Cash Equivalents                 | \$ 110.9            | \$ 246.1          |
| Accounts Receivable, Net                  | 229.8               | 202.6             |
| Inventories:                              |                     |                   |
| Finished Products                         | 27.3                | 15.4              |
| Work in Process                           | 9.4                 | 14.6              |
| Materials                                 | 81.6                | 54.1              |
| Total Inventories                         | 118.3               | 84.1              |
| Prepaid and Refundable Income Taxes       | 10.4                | 2.4               |
| Prepaid Expenses and Other Current Assets | 21.7                | 14.8              |
| Total Current Assets                      | 491.1               | 550.0             |
| Property Plan and Equipment:              |                     |                   |
| Land                                      | 3.6                 | 0.8               |
| Buildings and Building Improvements       | 73.8                | 69.2              |
| Machinery and Equipment                   | 382.9               | 364.7             |
| Property, Plant and Equipment, Gross      | 460.3               | 434.7             |
| Less: Allowances for Depreciation         | 272.4               | 272.5             |
| Property, Plant and Equipment, Net        | 187.9               | 162.2             |
| Other Assets:                             |                     |                   |
| Goodwill                                  | 233.9               | 59.2              |
| Other Intangible Assets, Net              | 275.1               | 61.0              |
| Cash Surrender Value of Life Insurance    | 8.5                 | 8.2               |
| Deferred Income Taxes                     | 32.7                | 42.3              |
| Pre-production Costs                      | 28.7                | 20.5              |
| Other                                     | 12.6                | 12.5              |
| Total Other Assets                        | 591.5               | 203.7             |
| Total Assets                              | \$ 1,270.5          | \$ 915.9          |
| Liabilities and Shareholders' Equity:     |                     |                   |
| Current Liabilities:                      |                     |                   |
| Accounts Payable                          | \$ 105.6            | \$ 89.5           |
| Salaries, Wages and Payroll Taxes         | 21.3                | 22.8              |
| Other Accrued Expenses                    | 33.2                | 21.6              |
| Short-term Debt                           | 15.3                | 4.4               |
| Income Tax Payable                        | 16.8                | 18.7              |
| Total Current Liabilities                 | 192.2               | 157.0             |
| Long-term Debt                            | 342.3               | 53.4              |
| Long-term Income Taxes Payable            | 38.9                | 42.6              |
| Other Liabilities                         | 4.2                 | 4.6               |
| Deferred Income Taxes                     | 39.8                | 18.3              |
| Deferred Compensation                     | 9.8                 | 10.0              |
| Total Liabilities                         | 627.2               | 285.9             |
| Shareholders' Equity:                     |                     |                   |

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|  |            |           |
|--|------------|-----------|
| Common Stock, \$0.50 par value, 100,000,000 shares authorized, 38,333,576 and 38,198,353 shares issued as of October 27, 2018 and April 28, 2018, respectively | 19.2       | 19.1      |
| Additional Paid-in Capital   | 147.3      | 136.5     |
| Accumulated Other Comprehensive Income (Loss)  | (11.7      | ) 13.9    |
| Treasury Stock, 1,346,624 shares as of October 27, 2018 and April 28, 2018   | (11.5      | ) (11.5 ) |
| Retained Earnings  | 500.0      | 472.0     |
| Total Shareholders' Equity   | 643.3      | 630.0     |
| Total Liabilities and Shareholders' Equity   | \$ 1,270.5 | \$ 915.9  |

See notes to condensed consolidated financial statements.

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METHODE ELECTRONICS, INC. AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)  
 (Dollars in millions)

|   | Six Months Ended |                  |
|---|------------------|------------------|
|   | October 2018     | October 28, 2017 |
| Operating Activities:   |                  |                  |
| Net Income  | \$38.3           | \$ 44.7          |
| Adjustments to Reconcile Net Income to Net Cash Provided by Operating Activities: |                  |                  |
| Gain on Sale of Fixed Assets  | (0.7 )           | —                |
| Provision for Depreciation  | 12.8             | 11.2             |
| Amortization of Intangible Assets   | 5.6              | 1.7              |
| Stock-based Compensation  | 10.9             | 7.2              |
| Provision for Bad Debt  | 0.1              | 0.1              |
| Change in Deferred Income Taxes   | (0.4 )           | —                |
| Changes in Operating Assets and Liabilities:                                      |                  |                  |
| Accounts Receivable   | (8.2 )           | (15.6 )          |
| Inventories   | (5.2 )           | (2.5 )           |
| Prepaid Expenses and Other Assets   | (13.0 )          | (3.5 )           |
| Accounts Payable and Other Expenses   | (4.0 )           | 1.9              |
| Net Cash Provided by Operating Activities   | 36.2             | 45.2             |
| Investing Activities:   |                  |                  |
| Purchases of Property, Plant and Equipment  | (28.6 )          | (16.4 )          |
| Acquisition of Business, Net of Cash Acquired                                     | (421.6 )         | (129.9 )         |
| Sale of Business/Investment/Property  | 0.7              | 0.3              |
| Net Cash Used in Investing Activities   | (449.5 )         | (146.0 )         |
| Financing Activities:   |                  |                  |
| Taxes Paid Related to Net Share Settlement of Equity Awards                       | (1.7 )           | (0.3 )           |
| Cash Dividends  | (8.6 )           | (6.8 )           |
| Proceeds from Borrowings  | 348.0            | 61.1             |
| Repayment of Borrowings   | (46.6 )          | (2.8 )           |
| Net Cash Provided by Financing Activities   | 291.1            | 51.2             |
| Effect of Foreign Currency Exchange Rate Changes on Cash                          | (13.0 )          | 14.2             |
| Increase (Decrease) in Cash and Cash Equivalents                                  | (135.2 )         | (35.4 )          |
| Cash and Cash Equivalents at Beginning of Year                                    | 246.1            | 294.0            |
| Cash and Cash Equivalents at End of Period  | \$110.9          | \$ 258.6         |
| See notes to condensed consolidated financial statements.                         |                  |                  |

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METHODE ELECTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in millions, except per share data)

1. BASIS OF PRESENTATION

Methode Electronics, Inc. was incorporated in 1946 as an Illinois corporation and reincorporated in Delaware in 1966. As used herein, “we,” “us,” “our,” the “Company” or “Methode” means Methode Electronics, Inc. and its subsidiaries. Our business is managed, and our financial results are reported, on a segment basis.

Effective October 27, 2018, the Company reorganized the reportable segments within its business to align to its new structure resulting from the acquisition of Grakon Parent, Inc. (“Grakon”). Prior to this reorganization, the Company's four reportable segments were Automotive, Power, Interface and Other. As a result of this change, the Company's four reportable segments are now Automotive, Industrial, Interface and Medical. Historical information has been revised to reflect the new reportable segments. Refer to Note 5, “Goodwill and Intangible Assets,” and Note 9, “Segment Information,” for further information.

The condensed consolidated financial statements and related disclosures as of October 27, 2018 and results of operations for the three and six months ended October 27, 2018 and October 28, 2017 are unaudited, pursuant to the rules and regulations of the Securities and Exchange Commission (“SEC”). The April 28, 2018 condensed consolidated balance sheet was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America (“U.S. GAAP”). Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to such rules and regulations. In our opinion, these financial statements include all adjustments (consisting only of normal recurring adjustments) necessary for the fair statement of the results for the interim periods. These financial statements should be read in conjunction with the financial statements included in our Form 10-K for the year ended April 28, 2018, filed with the SEC on June 21, 2018. Results may vary from quarter-to-quarter for reasons other than seasonality.

2. RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In February 2018, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) No. 2018-02, “Income Statement—Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income.” The amendments in this update are intended to address a specific consequence of the Tax Cuts and Jobs Act (“U.S. Tax Reform”) by allowing a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from U.S. Tax Reform’s reduction of the U.S. federal corporate income tax rate. The ASU is effective for all entities for annual periods beginning after December 15, 2018, with early adoption permitted, and is to be applied either in the period of adoption or retrospectively to each period in which the effect of the change in the U.S. federal corporate income tax rate is recognized. For Methode, the amendments in this update will be effective for our fiscal 2020, beginning on April 28, 2019. Management does not expect this ASU to have a material impact on the Company’s consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, “Leases (ASC 842),” which sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract (i.e. lessees and lessors). The new standard requires lessors to account for leases using an approach that is substantially equivalent to existing guidance for sales-type leases, direct financing leases and operating leases. The new standard requires lessees to apply a dual approach, classifying leases as either finance or operating leases based on the principle of whether or not the lease is effectively a financed purchase by the lessee. This classification will determine whether lease expense is recognized based on an effective interest method or on a straight line basis over the term of the lease. A lessee is also required to record a right-of-use asset and a lease liability for all leases with a term of greater than 12 months regardless of their classification. Leases with a term of 12 months or less will be accounted for similar to existing guidance for operating leases today. Accounting Standards Codification (“ASC”) 842 supersedes the previous leases standard, ASC 840 Leases. The amendments in this update are effective for fiscal years beginning after December 15, 2018, which is our fiscal 2020, beginning on April 28, 2019. This ASU is required to be applied with a modified

retrospective approach and requires application of the new standard at the beginning of the earliest comparative period presented.

In July 2018, the FASB issued ASU No. 2018-11, "Leases (Topic 842): Targeted Improvements." In issuing ASU No. 2018-11, the FASB decided to provide another transition method in addition to the existing transition method by allowing entities to initially apply the new leases standard at the adoption date and recognize a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption. The Company will elect this optional transition method to recognize a cumulative effect adjustment to the opening balance of retained earnings on April 27, 2019.

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METHODE ELECTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in millions, except per share data)

We are continuing to assess the accounting and disclosure impact of ASU 2016-02 and refine our processes for adoption on April 27, 2019. We expect the primary impact to our consolidated financial position upon adoption will be the recognition, on a discounted basis, of our minimum commitments under non-cancelable operating leases on our consolidated balance sheets resulting in the recording of right of use assets and lease obligations. Our minimum commitments under non-cancelable operating leases are not significantly different than those disclosed in our fiscal 2018 Form 10-K. As part of our adoption of this standard, we are currently in the process of selecting a software solution to assist in managing our inventory of leases and in complying with the disclosure requirements of this standard.

RECENTLY ADOPTED ACCOUNTING PRONOUNCEMENTS

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers," which created ASC 606 "Revenue from Contracts with Customers" ("ASC 606") and supersedes the revenue recognition requirements in ASC 605 "Revenue Recognition" ("ASC 605"). The guidance in ASU No. 2014-09 and subsequently issued amendments outlines a comprehensive model for all entities to use in accounting for revenue arising from contracts with customers as well as required disclosures. Under the new standard, recognition of revenue occurs when a customer obtains control of promised goods or services in an amount that reflects the consideration which the entity expects to receive in exchange for those goods or services. The new standard requires additional disclosure of the nature, amount, timing, and uncertainty of revenue and cash flows arising from contracts with customers including significant judgments and changes in judgments. We adopted the new standard effective April 29, 2018 using the modified retrospective transition method with the cumulative effect recorded to the opening balance of retained earnings as of the date of adoption. See Note 3, "Revenue" for further details.

In January 2016, the FASB issued ASU No. 2016-01, "Financial Instruments - Overall: Recognition and Measurement of Financial Assets and Financial Liabilities." The new standard requires equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income, requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes, requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset, and eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost. The standard was adopted by Methode on April 29, 2018 and did not have a material impact on our consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, "Statement of Cash Flows (Topic 230) - Classification of Certain Cash Receipts and Cash Payments." The amendments in this update provide guidance on eight specific cash flow presentation issues that have developed due to diversity in practice. The issues include, but are not limited to, debt prepayment or extinguishment costs, contingent consideration payments made after a business combination, and proceeds from the settlement of insurance claims. The amendments in this ASU, where practicable, are to be applied retrospectively. The standard was adopted by Methode on April 29, 2018 and did not have a material impact on our consolidated financial statements.

In May 2017, the FASB issued ASU No. 2017-09, "Compensation—Stock Compensation (Topic 718): Scope of Modification Accounting." The amendments in this update provide guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting in Topic 718. The standard was adopted by Methode on April 29, 2018 and did not have a material impact on our consolidated financial statements.

3. REVENUE

The Company is a global manufacturer of component and subsystem devices whose components are found in the primary end-markets of the aerospace, appliance, automotive, construction, consumer and industrial equipment, communications (including information processing and storage, networking equipment and wireless and terrestrial voice/data systems), medical, rail and other transportation industries. On April 29, 2018, we adopted ASC 606 along with the related amendments using a modified retrospective approach to all contracts open as of that date. Upon adoption, we recognized a \$0.1 million increase to opening retained earnings. This adjustment was a result of modifying our revenue recognition pattern for highly customized goods with no alternative use to over time recognition instead of point in time and for deferring revenue related to material rights that we provide to our customers. The overall impact to our financial statements was immaterial. We have modified our controls to address the risks present under ASC 606.

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## METHODE ELECTRONICS, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in millions, except per share data)

As we have adopted ASC 606 using the modified retrospective approach, our prior periods have not been restated, and as such they are presented under ASC 605. The impact of the changes in accounting policy on our fiscal 2019 is provided below.

| (Dollars in Millions) | Impact of Changes in Accounting Policy |             |                       |                                   |             |                       |
|-----------------------|--|-------------|-----------------------|-----------------------------------|-------------|-----------------------|
|                       | Three Months Ended October 27, 2018    |             |                       | Six Months Ended October 27, 2018 |             |                       |
|                       | As Reported                            | Adjustments | Balance Under ASC 605 | As Reported                       | Adjustments | Balance Under ASC 605 |
| Net Sales             | \$264.0                                | \$ (8.9 )   | \$ 272.9              | \$487.4                           | \$ (16.0 )  | \$ 503.4              |
| Cost of Products Sold | \$193.2                                | \$ (8.8 )   | \$ 202.0              | \$356.5                           | \$ (16.0 )  | \$ 372.5              |
| Total Inventories     |  |             |                       | \$118.3                           | \$ (0.6 )   | \$ 118.9              |
| Contract Assets       |  |             |                       | \$0.9                             | \$ 0.9      | \$ —                  |
| Contract Liabilities  |  |             |                       | \$0.2                             | \$ 0.2      | \$ —                  |
| Retained Earnings     |  |             |                       | \$500.0                           | \$ 0.1      | \$ 499.9              |

## Revenue Accounting Policy:

In May 2014, the FASB issued ASC 606, which supersedes the revenue recognition requirements in ASC 605, and requires entities to recognize revenue when control of the promised goods or services is transferred to customers at an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services.

The Company adopted ASC 606 as of April 29, 2018 using the modified retrospective transition method. The cumulative effect of initially applying the new standard was recorded as an adjustment to the opening balance of retained earnings within our condensed consolidated balance sheets. In accordance with the modified retrospective transition method, the historical information within the financial statements has not been restated and continues to be reported under the accounting standard in effect for those periods. As a result, the Company has disclosed the accounting policies in effect prior to April 29, 2018, as well as the policies it has applied starting April 29, 2018.

## Periods prior to April 29, 2018

Revenue is recognized in accordance with ASC 605. Revenue is recognized upon either shipment or delivery (depending on shipping terms) of product to customers and is recorded net of returns, allowances, customer discounts, and incentives. Sales taxes collected from customers and remitted to governmental authorities are accounted for on a net (excluded from revenues) basis.

## Periods commencing on or after April 29, 2018

The majority of our revenue is recognized at a point in time. The Company has determined that the most definitive demonstration that control has transferred to a customer is physical shipment or delivery, depending on the contractual shipping terms, with the exception of consignment transactions. Consignment transactions are arrangements where the Company transfers product to a customer location but retains ownership and control of such product until it is used by the customer. Revenue for consignment arrangements is recognized upon the customer's usage.

Revenues associated with products which we believe have no alternative use, and where the Company has an enforceable right to payment, are recognized on an over time basis. In transition to ASC 606, the Company noted some customers ordered highly customized parts in which the Company was entitled to payment throughout the manufacturing process. In accordance with ASC 606, the Company has begun recognizing revenue over time for these customers as the performance obligation is satisfied. The Company believes the most faithful depiction of the transfer of goods to the customer is based on progress to date, which is typically smooth throughout the production process. As such, the Company recognizes revenue evenly over the production process through transfer of control to the customer.

In addition, customers typically negotiate annual price downs. Management has evaluated these price downs and determined that in some instances, these price downs give rise to a material right. In instances that a material right exists, a portion of the transaction price is allocated to the material right and recognized over the life of the contract.

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METHODE ELECTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in millions, except per share data)

Our warranties are standard, assurance-type warranties only. We do not offer any additional service or extended term warranties to our customers. As such, we continue to recognize warranty as an expense with accounting outside of the scope of ASC 606.

The Company has elected to treat shipping and handling costs as an activity necessary to fulfill the performance obligation to transfer product to the customer and not as a separate performance obligation. Shipping and handling costs are estimated at quarter end in proportion to revenue recognized for transactions where actual costs are not yet known.

Across all products, the amount of revenue recognized corresponds to the related purchase order. Revenue is adjusted for variable consideration (such as discounts) as described further below. Sales and other taxes collected concurrent with revenue-producing activities are excluded from revenue.

The Company's performance obligations are typically short-term in nature. As a result, the Company has elected the practical expedient that provides an exemption from the disclosure requirements regarding information about remaining performance obligations on contracts that have original expected durations of one year or less.

Costs to Fulfill/Obtain a Contract:

We incur pre-production tooling costs related to products produced for our customers under long-term supply agreements. We had \$28.7 million and \$20.5 million as of October 27, 2018 and April 28, 2018, respectively, of pre-production tooling costs related to customer-owned tools for which reimbursement is contractually guaranteed by the customer or for which the customer has provided a non-cancelable right to use the tooling. These costs are capitalized and recognized into income upon acceptance. The Company concluded that pre-production tooling and engineering costs do not represent a promised good or service under ASC 606, and as such, reimbursements received are accounted for as a reimbursement of the expense, not revenue. This change resulted in tooling reimbursements of \$8.8 million and \$16.1 million being recorded into cost of products sold during the three and six months ended October 27, 2018, respectively.

The Company has not historically incurred material costs to obtain a contract. In the instances that costs to obtain contracts are incurred, the Company will capitalize and amortize those over the life of the contract.

Contract Estimates:

Due to the nature of the work performed in completing certain performance obligations, the estimation of both total revenue and cost at completion includes a number of variables and requires significant judgment.

Estimating total contract revenue may require judgment as certain contracts contain pricing discount structures, early payment discounts or other provisions that can impact the transaction price. The Company generally estimates variable consideration utilizing the most likely amount to which we expect to be entitled. When the contract provides the customer with the right to return eligible products, the Company reduces revenue at the point of sale using current facts and historical experience by using an estimate for expected product returns. The Company adjusts these estimates at the earlier of when the most likely amount of consideration that is expected to be received changes or when the consideration becomes fixed. Accordingly, an increase or decrease to revenue is recognized at that time. The Company has elected the practical expedient for significant financing components, allowing the Company to not adjust the promised amount of consideration for the effects of a financing component when payment terms are within



one year from the time a performance obligation is satisfied. Our customers' payment terms are typically 30-45 days from the time control transfers.

Certain of the Company's contracts contain annual contractually-guaranteed price reductions that grant the customer the right to purchase products at decreased prices throughout the life of the contract. Most of these contractual price reductions are merely the result of efficiencies in the production process being passed down to our customers. For certain of these price reductions, however, the amount of the reduction cannot be attributed entirely to production efficiencies gained. In these cases, the annual price-downs are considered to be material rights as the customer, as part of their current contract, is purchasing an option that they would not have received without the contract to purchase future product. When a contract contains a material right, a portion of the transaction price is allocated to the material right for which revenue recognition is deferred until the customer exercises its option. The standalone selling price for a material right used to allocate the transaction price is determined at contract inception by calculating the portion of the option purchased relative to the estimated total amount of incremental value the customer will likely earn, based on historical data, customer forecast communications, current economic

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METHODE ELECTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in millions, except per share data)

information and industry trends. The standalone selling price of a material right is not adjusted prior to customer exercise or option expiration.

Estimating the total expected costs related to contracts also requires significant judgment. In cases where the Company is recognizing revenue over time, the requirement is to record a proportionate amount of the costs of production as well. As part of this process, management considers the progress towards completion of the performance obligation, the length of time necessary to complete the performance obligation and the historical costs incurred in the manufacture of similar products, among other variables.

The Company has elected the portfolio approach practical expedient to estimate the amount of revenue to recognize for certain contracts which require over time revenue recognition. Such contracts are grouped together either by revenue stream, customer or product. Each portfolio of contracts is grouped together based on having similar characteristics. The portfolio approach is utilized only when the result of the accounting is not expected to be materially different than if applied to individual contracts. For each portfolio of contracts, the respective work in process and/or finished goods inventory balances are identified and the portfolio-specific margin is applied to estimate the pro-rata portion of revenue earned in relation to the costs incurred.

Adjustments due to any of the factors above to net sales, cost of sales and the related impact to operating income are recognized as necessary in the period they become known. The resultant impacts from these changes in estimates are recognized on a cumulative catch-up basis, which recognizes in the current period the cumulative effect of the changes on both current and prior periods.

**Contract Balances:**

The Company receives payment from customers based on the contractual billing schedule and specific performance requirements established in the contract. Billings are recorded as accounts receivable when an unconditional right to the contractual consideration exists. A contract asset is an entity's right to consideration in exchange for goods or services that the entity has transferred to a customer. A contract liability exists when the Company has received consideration or the amount is due from the customer in advance of revenue recognition. Contract assets and contract liabilities are recognized in other current assets and other liabilities, respectively, in the Company's condensed consolidated balance sheets.

Unbilled Receivables (Contract Assets) - Pursuant to the over time revenue recognition model, revenue may be recognized prior to the customer being invoiced. An unbilled receivable is recorded to reflect revenue that is recognized over time. The Company has determined that unbilled receivables were \$0.8 million and \$0.9 million as of April 29, 2018 and October 27, 2018, respectively. During the six months ended October 27, 2018, \$0.8 million of previously unbilled receivables were recorded into accounts receivable. There were no impairments of contract assets as of October 27, 2018.

Deferred Revenue (Contract Liabilities) - For certain of the price reductions offered by the Company, the amount of the reduction cannot be attributed entirely to production efficiencies gained. In these cases, the annual price-downs are considered to be material rights as the customer, as part of their current contract, are purchasing an option that they would not have received without the contract to purchase future product. When a contract contains a material right, a portion of the transaction price is allocated to the material right for which revenue recognition is deferred until the customer exercises its option. Deferred revenue was \$0.2 million at both April 29, 2018 and October 27, 2018. No previously deferred revenue was recorded into revenue during the six months ended October 27, 2018.



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## METHODE ELECTRONICS, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in millions, except per share data)

## Disaggregated Revenue Information:

The Company views the following disaggregated disclosures as useful to understanding the composition of revenue recognized during the respective reporting periods. Geographic net sales are determined based on our sales from our various operational locations. Though revenue recognition patterns and contracts are generally consistent, the amount, timing and uncertainty of revenue and cash flows may vary in each reportable segment due to geographic and economic factors.

|                       | Three Months Ended October 27, 2018 |            |         |           |         |
|-----------------------|-------------------------------------|------------|---------|-----------|---------|
|                       | Auto                                | Industrial | Medical | Interface | Total   |
| Geographic Net Sales: |                                     |            |         |           |         |
| U.S.                  | \$96.7                              | \$ 24.9    | \$ 0.3  | \$ 14.4   | \$136.3 |
| Malta                 | 29.6                                | 7.4        | —       | —         | 37.0    |
| China                 | 22.5                                | 9.1        | —       | 0.1       | 31.7    |
| Canada                | 24.3                                | 2.5        | —       | —         | 26.8    |
| Egypt                 | 12.9                                | —          | —       | —         | 12.9    |
| Belgium               | 8.7                                 | —          | —       | —         | 8.7     |
| Other                 | 6.9                                 | 3.5        | —       | 0.2       | 10.6    |
| Total Net Sales       | \$201.6                             | \$ 47.4    | \$ 0.3  | \$ 14.7   | \$264.0 |

## Timing of Revenue Recognition:

|                                      |         |         |        |         |         |
|--------------------------------------|---------|---------|--------|---------|---------|
| Goods Transferred at a Point in Time | \$193.6 | \$ 47.4 | \$ 0.3 | \$ 14.7 | \$256.0 |
| Goods Transferred Over Time          | 8.0     | —       | —      | —       | 8.0     |
| Total Net Sales                      | \$201.6 | \$ 47.4 | \$ 0.3 | \$ 14.7 | \$264.0 |

## Six Months Ended October 27, 2018

|                       | Six Months Ended October 27, 2018 |            |         |           |         |
|-----------------------|-----------------------------------|------------|---------|-----------|---------|
|                       | Auto                              | Industrial | Medical | Interface | Total   |
| Geographic Net Sales: |                                   |            |         |           |         |
| U.S.                  | \$174.0                           | \$ 37.0    | \$ 0.6  | \$ 29.4   | \$241.0 |
| Malta                 | 60.1                              | 15.7       | —       | 0.1       | 75.9    |
| China                 | 42.5                              | 17.9       | —       | 0.1       | 60.5    |
| Canada                | 45.1                              | 2.5        | —       | —         | 47.6    |
| Egypt                 | 25.6                              | —          | —       | —         | 25.6    |
| Belgium               | 17.0                              | —          | —       | —         | 17.0    |
| Other                 | 12.6                              | 6.5        | —       | 0.7       | 19.8    |
| Total Net Sales       | \$376.9                           | \$ 79.6    | \$ 0.6  | \$ 30.3   | \$487.4 |

## Timing of Revenue Recognition:

|                                      |         |         |        |         |         |
|--------------------------------------|---------|---------|--------|---------|---------|
| Goods Transferred at a Point in Time | \$359.1 | \$ 79.6 | \$ 0.6 | \$ 30.3 | \$469.6 |
| Goods Transferred Over Time          | 17.8    | —       | —      | —       | 17.8    |
| Total Net Sales                      | \$376.9 | \$ 79.6 | \$ 0.6 | \$ 30.3 | \$487.4 |

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## METHODE ELECTRONICS, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in millions, except per share data)

## 4. ACQUISITIONS

## Fiscal 2019 Acquisitions

## Grakon Parent, Inc.

On September 12, 2018, we acquired 100% of the stock of Grakon for 421.6 million in cash, net of cash acquired. The business, headquartered in Seattle, Washington, is a manufacturer of custom designed lighting solutions and highly styled engineered components. Grakon's manufacturing capabilities and products will help diversify our product offerings and expand the Industrial segment, which is a key component of our strategic direction. The accounts and transactions of Grakon have been included in the Automotive and Industrial segments in the consolidated financial statements from the effective date of the acquisition. For goodwill impairment testing purposes, Grakon has been included in the Company's North American Auto and Industrial reporting units.

The Company has not yet completed the process of estimating the fair value of any of the Grakon assets acquired and liabilities assumed. Accordingly, the Company's preliminary estimates and the allocation of the purchase price to the assets acquired and liabilities assumed may change as the Company completes the process, which would likely impact the Company's allocation of the purchase price to goodwill. The preliminary allocation of the purchase price to the fair values of the assets acquired and liabilities assumed were:

(Dollars in Millions)

|   |         |
|---|---------|
| Cash                                      | \$6.9   |
| Accounts Receivable                       | 36.1    |
| Inventory                                 | 31.0    |
| Prepaid Expenses and Other Current Assets | 1.2     |
| Intangible Assets                         | 220.9   |
| Goodwill                                  | 175.2   |
| Pre-Production Costs                      | 1.5     |
| Property, Plant and Equipment             | 18.0    |
| Accounts Payable                          | (19.4 ) |
| Salaries, Wages and Payroll Taxes         | (4.4 )  |
| Other Accrued Expenses                    | (7.2 )  |
| Income Taxes Payable                      | (0.7 )  |
| Deferred Income Tax Liability             | (30.6 ) |
| Total Purchase Price                      | \$428.5 |

The following table presents details of the intangible assets acquired:

| (Dollars in Millions)  | Fair Value<br>at Date of<br>Acquisition | Amortization Period |
|--|---|---------------------|
| Customer Relationships and Agreements - Significant Customer | \$ 56.0                                 | 19.5 years          |
| Customer Relationships and Agreements - All Other Customers  | 125.0                                   | 19.5 years          |
| Technology Licenses  | 17.7                                    | 6.3 years           |
| Trade Names  | 22.2                                    | 8.5 years           |
| Total  | \$ 220.9                                |                     |

The Company's results of operations for the three and six months ended October 27, 2018 included approximately one and a half months of the operating results of Grakon, which was comprised of revenues of \$24.2 million and net loss

of \$0.2 million.

Acquisition-related costs of \$10.9 million and \$11.5 million were incurred in relation to the acquisition of Grakon for the three and six months ended October 27, 2018, respectively. Acquisition-related costs for the three months ended October

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## METHODE ELECTRONICS, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in millions, except per share data)

27, 2018 included \$8.3 million of costs which have been reported in selling and administrative expenses and \$2.6 million of costs which have been reported in costs of products sold on the condensed consolidated statements of income. Acquisition-related costs for the six months ended October 27, 2018 included \$8.9 million of costs which have been reported in selling and administrative expenses and \$2.6 million of costs which have been reported in costs of products sold on the condensed consolidated statements of income.

## Fiscal 2018 Acquisitions

## Procoplast S.A.

On July 27, 2017, we acquired 100% of the stock of Procoplast S.A. ("Procoplast") for \$22.2 million in cash, net of cash acquired. The business, located near the Belgian-German border, is an independent manufacturer of automotive assemblies. The accounts and transactions of Procoplast have been included in the Automotive segment in the consolidated financial statements from the effective date of the acquisition. For goodwill impairment testing purposes, Procoplast has been included in the Company's European Automotive reporting unit.

During the fourth quarter of fiscal 2018, the Company completed the allocation of the purchase price to the assets acquired and liabilities assumed. The final allocation of the purchase price to the fair values of the assets acquired and liabilities assumed was:

(Dollars in Millions)

|                                   |         |
|-----------------------------------|---------|
| Cash                              | \$1.3   |
| Accounts Receivable               | 7.4     |
| Inventory                         | 3.5     |
| Intangible Assets                 | 19.2    |
| Goodwill                          | 6.8     |
| Pre-Production Costs              | 2.3     |
| Property, Plant and Equipment     | 23.8    |
| Accounts Payable                  | (4.9 )  |
| Salaries, Wages and Payroll Taxes | (0.8 )  |
| Other Accrued Expenses            | (0.7 )  |
| Income Taxes Payable              | (0.6 )  |
| Short-term Debt                   | (3.2 )  |
| Other Liabilities                 | (2.1 )  |
| Long-term Debt                    | (20.6 ) |
| Deferred Income Tax Liability     | (7.9 )  |
| Total Purchase Price              | \$23.5  |

The following table presents details of the intangible assets acquired:

| (Dollars in Millions)  | Fair Value<br>at Date of<br>Acquisition | Amortization Period |
|--|---|---------------------|
| Customer Relationships and Agreements - Significant Customer | \$ 12.3                                 | 17.0 years          |
| Customer Relationships and Agreements - All Other Customers  | 2.8                                     | 11.5 years          |
| Technology Licenses  | 2.1                                     | 8.5 years           |
| Trade Names  | 2.0                                     | 8.5 years           |

Total

\$ 19.2

Acquisition-related costs of \$0.2 million and \$1.3 million were incurred in relation to the acquisition of Procoplast for the three and six months ended October 28, 2017, respectively. Acquisition-related costs for the three months ended

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## METHODE ELECTRONICS, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in millions, except per share data)

October 28, 2017 included \$0.2 million of costs which have been reported in costs of products sold on the condensed consolidated statements of income. Acquisition costs for the six months ended October 28, 2017 included \$1.1 million of costs which have been reported in selling and administrative expenses and \$0.2 million of costs which have been reported in costs of products sold on the condensed consolidated statements of income.

## Pacific Insight Electronics Corp.

On October 3, 2017, we acquired 100% of the outstanding common shares of Pacific Insight Electronics Corp. ("Pacific Insight") in a cash transaction for \$108.7 million, net of cash acquired. Pacific Insight, headquartered in Vancouver, British Columbia, Canada, is a global solutions provider offering design, development, manufacturing and delivery of lighting and electronic products and full-service solutions to the automotive and commercial vehicle markets, and has manufacturing facilities in both Canada and Mexico. Its technology in LED-based ambient and direct lighting will expand our presence within the automotive interior, as well as augment our efforts in overhead console and other areas. The accounts and transactions of Pacific Insight have been included in the Automotive segment in the consolidated financial statements from the effective date of the acquisition. For goodwill impairment testing purposes, Pacific Insight has been included in the Company's North American Automotive reporting unit.

During the fourth quarter of fiscal 2018, the Company completed the allocation of the purchase price to the assets acquired and liabilities assumed. The final allocation of the purchase price to the fair values of the assets acquired and liabilities assumed was:

(Dollars in Millions)

|   |         |
|---|---------|
| Cash                                      | \$4.9   |
| Accounts Receivable                       | 18.3    |
| Inventory                                 | 13.0    |
| Prepaid Expenses and Other Current Assets | 0.3     |
| Income Taxes Receivable                   | 1.2     |
| Intangible Assets                         | 40.1    |
| Goodwill                                  | 50.4    |
| Pre-production Costs                      | 0.8     |
| Property, Plant and Equipment             | 13.2    |
| Accounts Payable                          | (7.9 )  |
| Salaries, Wages and Payroll Taxes         | (0.8 )  |
| Other Accrued Expenses                    | (2.9 )  |
| Short-term Debt                           | (0.8 )  |
| Long-term Debt                            | (3.4 )  |
| Deferred Income Tax Liability             | (12.8 ) |
| Total Purchase Price                      | \$113.6 |

The following table presents details of the intangible assets acquired:

| (Dollars in Millions)                              | Fair Value<br>at Date of<br>Acquisition | Amortization Period |
|--|---|---------------------|
| Customer Relationships and Agreements - Automotive | \$ 22.6                                 | 11.0 years          |
| Customer Relationships and Agreements - Commercial | 9.6                                     | 13.0 years          |
| Trade Names  | 6.2                                     | 7.5 years           |
| Technology Licenses                                | 1.7                                     | 5.5 years           |

Total \$ 40.1

Acquisition-related costs of \$4.0 million and \$5.5 million were incurred in relation to the acquisition of Pacific Insight for the three and six months ended October 28, 2017, respectively. Acquisition-related costs for the three months ended

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## METHODE ELECTRONICS, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in millions, except per share data)

October 28, 2017 included \$3.4 million of costs which have been reported in selling and administrative expenses and \$0.6 million of costs which have been reported in costs of products sold on the condensed consolidated statements of income. Acquisition-related costs for the six months ended October 28, 2017 included \$4.9 million of costs which have been reported in selling and administrative expenses and \$0.6 million of costs which have been reported in costs of products sold on the condensed consolidated statements of income.

The following table presents unaudited supplemental pro forma results for the three and six months ended October 27, 2018 and October 28, 2017, respectively, as if both the Grakon acquisition had occurred as of the beginning of fiscal 2018 and the Pacific Insight acquisition had occurred as of the beginning of fiscal 2017. The unaudited pro forma information is presented for information purposes only and is not indicative of the results of operations that would have been achieved if the acquisitions had taken place at such times. The unaudited pro forma results presented below primarily include amortization charges for acquired intangible assets, depreciation adjustments for property, plant and equipment that has been revalued, interest expense adjustments due to an increased debt level, adjustments for certain acquisition-related charges and related tax effects.

| (Dollars in Millions) | (Unaudited)        |                  |                  |                  |
|-----------------------|--------------------|------------------|------------------|------------------|
|                       | Three Months Ended |                  | Six Months Ended |                  |
|                       | October 27, 2018   | October 28, 2017 | October 27, 2018 | October 28, 2017 |
| Revenues              | \$285.5            | \$ 284.3         | \$556.2          | \$ 543.4         |
| Net Income            | \$26.9             | \$ 30.3          | \$58.5           | \$ 57.1          |

## 5. GOODWILL AND INTANGIBLE ASSETS

We review our goodwill and other intangible assets for impairment whenever events or changes in circumstances indicate that the carrying amount of these assets may not be recoverable, and at least annually in accordance with ASC No. 350, "Intangibles — Goodwill and Others." The values assigned to goodwill and intangible assets are normally based on estimates and judgments regarding expectations for the success and life cycle of products and technologies acquired. A severe decline in expectations could result in significant impairment charges, which could have a material adverse effect on our financial condition and results of operations.

Effective October 27, 2018, the Company reorganized the reportable segments within its business to align to its new structure resulting from the acquisition of Grakon. Prior to this reorganization, the Company's four reportable segments were Automotive, Power, Interface and Other. As a result of this change, the Company's four reportable segments are now Automotive, Industrial, Interface and Medical. Historical information has been revised to reflect the new reportable segments. Refer to Note 9, "Segment Information," for further information.

As part of the acquisition of Grakon in fiscal 2019, the Company recorded goodwill of \$175.2 million, of which \$39.4 million is deductible for income taxes. As part of the acquisitions of Procoplast and Pacific Insight in fiscal 2018, the Company recorded goodwill of \$6.8 million and \$50.4 million, respectively, of which none is deductible for income taxes. The following table shows the roll-forward of goodwill in the financial statements as of October 27, 2018.

|                                | Automotive | Industrial | Total   |
|--------------------------------|------------|------------|---------|
| Balance as of April 28, 2018   | \$ 57.5    | \$ 1.7     | \$59.2  |
| Goodwill Acquired              | 49.9       | 125.3      | 175.2   |
| Foreign Currency Translation   | (0.5 )     | —          | (0.5 )  |
| Balance as of October 27, 2018 | \$ 106.9   | \$ 127.0   | \$233.9 |

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## METHODE ELECTRONICS, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in millions, except per share data)

As part of the acquisition of Grakon in fiscal 2019, the Company acquired estimated intangible assets of \$220.9 million. As part of the acquisitions of Procoplast and Pacific Insight in fiscal 2018, the Company acquired intangible assets of \$19.2 million and \$40.1 million, respectively. The following tables present details of the Company's intangible assets.

|  | As of October 27, 2018 |                          |         | Wtd. Avg. Remaining Amortization Periods (Years) |
|--|------------------------|--------------------------|---------|--|
|  | Gross                  | Accumulated Amortization | Net     |  |
| Customer Relationships and Agreements        | \$244.2                | \$ 21.2                  | \$223.0 | 17.9   |
| Trade Names, Patents and Technology Licenses | 77.5                   | 25.4                     | 52.1    | 6.9  |
| Total  | \$321.7                | \$ 46.6                  | \$275.1 |  |
|  | As of April 28, 2018   |                          |         | Wtd. Avg. Remaining Amortization Periods (Years) |
|  | Gross                  | Accumulated Amortization | Net     |  |
| Customer Relationships and Agreements        | \$64.4                 | \$ 18.1                  | \$46.3  | 12.3   |
| Trade Names, Patents and Technology Licenses | 37.7                   | 23.0                     | 14.7    | 5.3  |
| Total  | \$102.1                | \$ 41.1                  | \$61.0  |  |

The estimated aggregate amortization expense for the current fiscal year and each of the four succeeding fiscal years is as follows:

|      |        |
|------|--------|
| 2019 | \$16.6 |
| 2020 | \$20.2 |
| 2021 | \$20.1 |
| 2022 | \$20.1 |
| 2023 | \$20.1 |

As of October 27, 2018 and April 28, 2018, the trade names, patents and technology licenses include \$1.8 million of trade names that are not subject to amortization.

**6. INCOME TAXES**

The provision for income taxes for an interim period is based on an estimated effective income tax rate for the full fiscal year and applies that rate to ordinary year-to-date earnings or loss. The estimated annual effective income tax rate is determined excluding the effects of unusual or significant discrete items that are reported net of the related tax effects and in the period in which they occur. In addition, any effects of enacted tax law or rate changes as well as the Company's ability to utilize various tax assets is recognized in the period in which the change occurs.

The Company recognized an income tax provision of \$3.0 million and \$4.9 million for the three months ended October 27, 2018 and October 28, 2017, respectively. The Company's effective tax rate was 17.0% and 16.8% for the three months ended October 27, 2018 and October 28, 2017, respectively. The Company recognized an income tax provision of \$7.5 million and \$9.2 million for the six months ended October 27, 2018 and October 28, 2017, respectively. The Company's effective tax rate was 16.4% and 17.1% for the six months ended October 27, 2018 and October 28, 2017, respectively.

The income tax provision for both the three and six months ended October 27, 2018 is lower than the U.S. statutory tax rate primarily due to foreign investment tax credits, foreign operations with lower statutory rates and the deduction for stock compensation. The income tax provision for both the three and six months ended and October 28, 2017 is lower than the U.S. statutory tax rate primarily due to foreign investment tax credits, foreign operations with lower statutory rates and a change in the Illinois state tax rate.



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## METHODE ELECTRONICS, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in millions, except per share data)

Additionally, the Company's tax rate was impacted by U.S. Tax Reform, which was enacted on December 22, 2017. U.S. Tax Reform provided for a reduction of the U.S. federal corporate income tax rate from 35% to 21%, effective January 1, 2018. The SEC staff issued Staff Accounting Bulletin ("SAB") 118 to provide certain guidance in determining the accounting for income tax effects of the legislation in the accounting period of enactment as well as provide a one-year measurement period to finalize the effects associated with U.S. Tax Reform. In the three months ended October 27, 2018, there has not been a re-measurement associated with the transition tax provisions associated with U.S. Tax Reform. The Company will update and finalize the accounting for the tax effects of the enactment of U.S. Tax Reform in the third quarter as determined and in accordance with the guidance as outlined in SAB 118.

## 7. COMMON STOCK AND STOCK-BASED COMPENSATION

## Restricted Stock Awards ("RSAs")

In fiscal 2016, the Compensation Committee of the Board of Directors authorized a new long-term incentive program (the "LTIP") for key employees consisting of performance-based restricted stock awards ("RSAs") and time-based restricted stock units ("RSUs"). Additionally, in the first quarter of fiscal 2019, the Compensation Committee awarded a maximum of 11,625 RSAs to an additional key member of management under the LTIP.

In the aggregate, the number of RSAs earned will vary based on performance relative to established goals for fiscal 2020 EBITDA, with 50% of the target shares earned for threshold performance (representing 344,418 shares), 100% of the target shares earned for target performance (representing 688,836 shares) and 150% of the target shares earned for maximum performance (representing 1,033,253 shares). Starting in the third quarter of fiscal 2018 and ending with the first quarter of fiscal 2019, the Company had been recording the RSA compensation expense based on threshold performance. Prior thereto, the Company had been recording the RSA compensation expense based on target performance.

Per ASC 718 accounting guidance, management is required in each reporting period to determine the fiscal 2020 EBITDA level that is "probable" (70% confidence) for which a performance condition will be achieved. Due to the expected accretive nature of the Grakon acquisition on 2020 results, management determined during the second quarter of fiscal 2019 that it was probable that the Company will meet the fiscal 2020 target consolidated EBITDA performance level of \$221.0 million.

At the target level of performance, the expected expense for the RSAs is \$22.9 million through fiscal 2020. In the three and six months ended October 27, 2018, the Company recorded \$8.1 million and \$9.1 million, respectively, in compensation expense related to the RSAs based on target levels which included an additional expense of \$7.4 million as a result of changing the estimated level of performance from threshold to target levels. During the three and six months ended October 28, 2017, the Company recorded \$1.7 million and \$3.2 million, respectively, in compensation expense related to the RSAs, based on target levels.

In future reporting periods, if management makes a determination that exceeding the target level is probable for fiscal 2020, an appropriate adjustment to compensation expense will be recorded in that period. In addition, if management makes a determination that it is not probable the Company will meet the target level for fiscal 2020, a reversal of compensation expense will be recorded in that period. The adjustments could be material to the financial statements.

## Restricted Stock Units ("RSUs")

In the first quarter of fiscal 2019, the Compensation Committee awarded 7,750 RSUs to Methode management. In the aggregate, the Company has granted 646,675 RSUs to key employees, of which 339,022 are still unvested and outstanding. The RSUs are subject to a vesting period, with 30% vested on April 28, 2018, 30% vesting on April 27, 2019 and 40% vesting on May 2, 2020. The total expense for the RSUs is expected to be \$17.6 million through fiscal 2020. During the three and six months ended October 27, 2018, the Company recorded \$0.8 million and \$0.9 million, respectively, of compensation expense related to the RSUs. During the three and six months ended October 28, 2017, the Company recorded \$1.5 million and \$3.0 million, respectively, in compensation expense related to the RSUs.

## Director Awards

During the first quarter of fiscal 2019, the Company issued 24,000 shares of common stock to our independent directors, all of which vested immediately upon grant. We recorded \$0.9 million of compensation expense related to these shares during the six months ended October 27, 2018.

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## METHODE ELECTRONICS, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in millions, except per share data)

## 8. NET INCOME PER SHARE

Basic net income per share is calculated by dividing net income by the weighted average number of common shares outstanding for the applicable period. Diluted net income per share is calculated after adjusting the denominator of the basic net income per share calculation for the effect of all potentially dilutive stock compensation awards outstanding during the period.

The following table sets forth the computation of basic and diluted net income per share:

|  | Three Months<br>Ended<br>October 27,<br>2018 |            | Six Months<br>Ended<br>October 27,<br>2018 |            |
|--|--|------------|--|------------|
| Numerator - Net Income   | \$ 14.6                                      | \$ 24.2    | \$ 38.3                                    | \$ 44.7    |
| Denominator:   |  |            |  |            |
| Denominator for Basic Net Income per Share-Weighted Average Shares Outstanding and Vested/Unissued Restricted Stock Awards | 37,405,375                                   | 37,083,500 | 37,377,379                                 | 37,266,095 |
| Dilutive Potential Common Shares-Employee Stock Options, Restricted Stock Awards and Restricted Stock Units                | 268,173                                      | 384,600    | 270,051                                    | 363,545    |
| Denominator for Diluted Net Income per Share   | 37,673,548                                   | 37,468,100 | 37,647,430                                 | 37,629,640 |
| Net Income per Share:  |  |            |  |            |
| Basic  | \$ 0.39                                      | \$ 0.65    | \$ 1.02                                    | \$ 1.20    |
| Diluted  | \$ 0.39                                      | \$ 0.64    | \$ 1.02                                    | \$ 1.19    |

For the three months ended October 27, 2018, 109,168 options have been excluded in the computation of diluted net income per share because the average market price was greater than the exercise price for the period. For the six months ended October 27, 2018, no options have been excluded in the computation of diluted net income per share because the average market price was greater than the exercise price for the period. RSAs for 688,835 and 523,684 shares have been excluded in the computation of diluted net income per share for the three and six months ended October 27, 2018, respectively, as these awards are contingent on the Company's full-year performance in fiscal 2020. For the three and six months ended October 28, 2017, no options have been excluded in the computation of diluted net income per share because the average market price was greater than the exercise price for those periods. RSAs for 821,075 and 821,075 shares have been excluded in the computation of diluted net income per share for the three and six months ended October 28, 2017, respectively, as these awards are contingent on the Company's full-year performance in fiscal 2020.

## 9. SEGMENT INFORMATION

We are a global manufacturer of component and subsystem devices. We design, manufacture and market devices employing electrical, electronic, wireless, sensing and optical technologies. Our components are found in the primary end-markets of the automotive, appliance, communications (including information processing and storage, networking equipment and wireless and terrestrial voice/data systems), consumer and industrial equipment, aerospace, rail and other transportation industries.

ASC No. 280, "Segment Reporting" establishes annual and interim reporting standards for an enterprise's operating segments and related disclosures about its products, services, geographic areas and major customers. An operating segment is defined as a component of an enterprise that engages in business activities from which it may earn revenues and incur expenses, and about which separate financial information is regularly evaluated by the Chief Operating Decision Maker ("CODM") in deciding how to allocate resources. The CODM, as defined by ASC No. 280, is the Company's President and Chief Executive Officer ("CEO").



Effective October 27, 2018, the Company reorganized the reportable segments within its business to align to its new structure resulting from the acquisition of Grakon. Prior to this reorganization, the Company's four reportable segments were

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METHODE ELECTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in millions, except per share data)

Automotive, Power, Interface and Other. As a result of this change, the Company's four reportable segments are now Automotive, Industrial, Interface and Medical. Historical information has been revised to reflect the new reportable segments. Refer to Note 5, "Goodwill and Intangible Assets," for further information.

A summary of the significant reportable segment changes is as follows:

- Grakon's automotive business has been included in the Automotive segment, while Grakon's non-automotive business has been included in the Industrial segment.
- ¶ The busbar business, previously included in the Power segment, is now part of the Industrial segment.
- ¶ The radio-remote control business, previously included in the Interface segment, is now part of the Industrial segment.
- The medical devices business, previously included in the Other segment, now makes up the Medical segment.

The Automotive segment supplies electronic and electro-mechanical devices and related products to automobile OEMs, either directly or through their tiered suppliers. Our products include integrated center consoles, hidden switches, ergonomic switches, transmission lead-frames, LED-based lighting and sensors, which incorporate magneto-elastic sensing and other technologies that monitor the operation or status of a component or system.

The Industrial segment manufactures external lighting solutions, industrial safety radio remote controls, braided flexible cables, current-carrying laminated busbars and devices, custom power-product assemblies, such as our PowerRail® solution, high-current low-voltage flexible power cabling systems and powder-coated busbars that are used in various markets and applications, including aerospace, computers, industrial, power conversion, military, telecommunications and transportation.

The Interface segment provides a variety of copper and fiber-optic interface and interface solutions for the appliance, commercial food service, construction, consumer, material handling, medical, point-of-sale and telecommunications markets. Solutions include optical and copper transceivers and solid-state field-effect consumer touch panels.

The Medical segment is made up of our medical device business, Dabir Surfaces, our surface support technology aimed at pressure injury prevention. Methode is developing the technology for use by patients who are immobilized or otherwise at risk for pressure injuries, including patients undergoing long-duration surgical procedures.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies in our Form 10-K for the fiscal year ended April 28, 2018, with the exception of accounting policies for revenue, which can be found in Note 3, "Revenue," in this Form 10-Q. We allocate resources to segments based on operating income. Transfers between segments are recorded using internal transfer prices set by us.

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## METHODE ELECTRONICS, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in millions, except per share data)

The tables below present information about our reportable segments.

|                                     | Three Months Ended October 27, 2018 |            |           |           |                        | Consolidated |
|-------------------------------------|-------------------------------------|------------|-----------|-----------|------------------------|--------------|
|                                     | Automotive                          | Industrial | Interface | Medical   | Eliminations/Corporate |              |
| Net Sales                           | \$203.5                             | \$ 47.9    | \$ 14.7   | \$ 0.3    | \$ (2.4 )              | \$ 264.0     |
| Transfers between Segments          | (1.9 )                              | (0.5 )     | —         | —         | 2.4                    | —            |
| Net Sales to Unaffiliated Customers | \$201.6                             | \$ 47.4    | \$ 14.7   | \$ 0.3    | \$ —                   | \$ 264.0     |
| Income (Loss) from Operations       | \$36.8                              | \$ 5.1     | \$ (0.6 ) | \$ (2.5 ) | \$ (19.7 )             | \$ 19.1      |
| Gain on Sale of Business            |                                     |            |           |           |                        | —            |
| Interest Expense, Net               |                                     |            |           |           |                        | 1.6          |
| Other Income, Net                   |                                     |            |           |           |                        | (0.1 )       |
| Income before Income Taxes          |                                     |            |           |           |                        | \$ 17.6      |
|                                     | Three Months Ended October 28, 2017 |            |           |           |                        | Consolidated |
|                                     | Automotive                          | Industrial | Interface | Medical   | Eliminations/Corporate |              |
| Net Sales                           | \$188.8                             | \$ 24.6    | \$ 18.8   | \$ —      | \$ (2.1 )              | \$ 230.1     |
| Transfers between Segments          | (2.1 )                              | 0.1        | (0.1 )    | —         | 2.1                    | —            |
| Net Sales to Unaffiliated Customers | \$186.7                             | \$ 24.7    | \$ 18.7   | \$ —      | \$ —                   | \$ 230.1     |
| Income (Loss) from Operations       | \$42.9                              | \$ 2.7     | \$ 2.1    | \$ (3.1 ) | \$ (14.9 )             | \$ 29.7      |
| Interest Income, Net                |                                     |            |           |           |                        | 0.2          |
| Other Income, Net                   |                                     |            |           |           |                        | 0.4          |
| Income before Income Taxes          |                                     |            |           |           |                        | \$ 29.1      |
|                                     | Six Months Ended October 27, 2018   |            |           |           |                        | Consolidated |
|                                     | Automotive                          | Industrial | Interface | Medical   | Eliminations/Corporate |              |
| Net Sales                           | \$381.0                             | \$ 80.9    | \$ 30.4   | \$ 0.6    | \$ (5.5 )              | \$ 487.4     |
| Transfers between Segments          | (4.1 )                              | (1.3 )     | (0.1 )    | —         | 5.5                    | —            |
| Net Sales to Unaffiliated Customers | \$376.9                             | \$ 79.6    | \$ 30.3   | \$ 0.6    | \$ —                   | \$ 487.4     |
| Income (Loss) from Operations       | \$69.7                              | \$ 12.2    | \$ 0.2    | \$ (4.6 ) | \$ (29.7 )             | \$ 47.8      |
| Interest Expense, Net               |                                     |            |           |           |                        | 1.8          |
| Other Expense, Net                  |                                     |            |           |           |                        | 0.2          |
| Income before Income Taxes          |                                     |            |           |           |                        | \$ 45.8      |
|                                     | Six Months Ended October 28, 2017   |            |           |           |                        | Consolidated |
|                                     | Automotive                          | Industrial | Interface | Medical   | Eliminations/Corporate |              |
| Net Sales                           | \$347.7                             | \$ 50.2    | \$ 37.9   | \$ 0.1    | \$ (4.6 )              | \$ 431.3     |
| Transfers between Segments          | (4.5 )                              | 0.3        | (0.4 )    | —         | 4.6                    | —            |
| Net Sales to Unaffiliated Customers | \$343.2                             | \$ 50.5    | \$ 37.5   | \$ 0.1    | \$ —                   | \$ 431.3     |
| Income (Loss) from Operations       | \$78.7                              | \$ 5.1     | \$ 3.4    | \$ (5.8 ) | \$ (26.3 )             | \$ 55.1      |
| Other Expense, Net                  |                                     |            |           |           |                        | 1.2          |
| Income before Income Taxes          |                                     |            |           |           |                        | \$ 53.9      |

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METHODE ELECTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in millions, except per share data)

10. CONTINGENCIES

Certain litigation arising in the normal course of business is pending against us. We are, from time-to-time, subject to various legal actions and claims incidental to our business, including those arising out of alleged defects, breach of contracts, employment-related matters, environmental matters and intellectual property matters. We consider insurance coverage and third-party indemnification when determining required accruals for pending litigation and claims. Although the outcome of potential legal actions and claims cannot be determined, it is our opinion, based on the information available, that we have adequate reserves for these liabilities.

Hetronic Germany-GmbH Matters

For several years, Hetronic Germany-GmbH and Hydronic-Steuersysteme-GmbH (the “Fuchs companies”) served as our distributors for Germany, Austria and other central and eastern European countries pursuant to their respective intellectual property licenses and distribution and assembly agreements. We became aware that the Fuchs companies and their managing director, Albert Fuchs, had materially violated those agreements. As a result, we terminated all of our agreements with the Fuchs companies. On June 20, 2014, we filed a lawsuit against the Fuchs companies in the Federal District Court for the Western District of Oklahoma alleging material breaches of the distribution and assembly agreements and seeking damages, as well as various forms of injunctive relief. The defendants have filed counterclaims alleging breach of contract, interference with business relations and business slander. On April 2, 2015, we amended our complaint against the Fuchs companies to add additional unfair competition and Lanham Act claims and to add additional affiliated parties. As of October 27, 2018, the matter remains in the pre-trial stage.

11. PRE-PRODUCTION COSTS RELATED TO LONG-TERM SUPPLY ARRANGEMENTS

We incur pre-production tooling costs related to certain products produced for our customers under long-term supply agreements. We had \$28.7 million and \$20.5 million as of October 27, 2018 and April 28, 2018, respectively, of pre-production tooling costs related to customer-owned tools for which reimbursement is contractually guaranteed by the customer or for which the customer has provided a non-cancelable right to use the tooling. Engineering, testing and other costs incurred in the design and development of production parts are expensed as incurred, unless the costs are reimbursable, as specified in a customer contract. We had \$8.9 million and \$10.1 million at October 27, 2018 and April 28, 2018, respectively, of Company owned pre-production tooling, which is capitalized within property, plant and equipment.

12. DEBT

On September 12, 2018, the Company entered into an Amended and Restated Credit Agreement with Bank of America, N.A., as Administrative Agent, Swing Line Lender and L/C Issuer, Wells Fargo Bank, National Association, as L/C Issuer, and the Lenders named therein (the “Credit Agreement”). The Credit Agreement amends and restates the Credit Agreement, dated November 18, 2016 (the “Existing Credit Agreement”), among the Company, Bank of America, N.A., as Administrative Agent, Swing Line Lender, and L/C Issuer, Wells Fargo Bank, National Association, as L/C Issuer, and the Lenders named therein. The Credit Agreement has a maturity date of September 12, 2023. The Credit Agreement includes a senior unsecured revolving credit facility, as well as a senior unsecured term loan, and is guaranteed by the Company’s wholly-owned U.S. subsidiaries.

The revolving credit facility has a maximum principal amount of \$200.0 million and is available for general corporate purposes, including working capital and acquisitions. The term loan has a principal amount of \$250.0 million, which is to be repaid in equal installments over the five-year term, and was made to partially fund the acquisition of Grakon in the second quarter of fiscal 2019. The Credit Agreement contains an option to increase the aggregate principal amount of the revolving credit facility and term loan by up to an additional \$200.0 million, subject to customary conditions and approval of the lender(s) providing new commitment(s). The Credit Agreement provides for variable rates of interest based on the type of borrowing and the Company's debt to EBITDA financial ratio and contains customary representations and warranties, financial covenants, restrictive covenants and events of default. At October 27, 2018, the interest rate on both the revolving credit facility and term loan was 1.50% plus LIBOR and we were in compliance with the covenants of the agreement. During the six months ended October 27, 2018, we had

\$348.0 million of borrowings, including the \$250.0 million term loan, and payments of \$41.5 million, which includes interest of \$1.5 million, under the Credit Agreement. As of October 27, 2018, there were outstanding balances of \$88.0 million and \$250.0 million against the revolving credit facility and term loan, respectively. We believe the fair values approximate the carrying amounts as of October 27, 2018.

Methode's subsidiary, Pacific Insight, is party to a credit agreement with the Bank of Montreal. The credit agreement with the Bank of Montreal has a maturity date of December 21, 2019 and provides a credit facility in the maximum principal

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METHODE ELECTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in millions, except per share data)

amount of C\$10.0 million, with an option to increase the principal amount by up to an additional C\$5.0 million. Availability under the facility is determined based upon a percentage of eligible accounts receivable and finished goods inventory balances and funds are available in either Canadian or U.S. currency. Interest is calculated at either the Canadian Dollar Offered Rate plus 1.25%, the Federal Funds Rate plus 1.25% or LIBOR plus 1.75%. As of October 27, 2018, there were no outstanding balances against this credit facility and Pacific Insight was in compliance with the covenants of the agreement.

In addition to the credit agreement with the Bank of Montreal, Pacific Insight was, until the second quarter of fiscal 2019, party to a credit agreement with Roynat. The credit agreement between Pacific Insight and Roynat was terminated during the second quarter of fiscal 2019 and payments of \$2.8 million were made upon termination, including a prepayment fee of \$0.1 million. Total repayments under this credit facility in fiscal 2019 were \$3.8 million.

Excluding credit facilities, the Company also holds debt at its Procoplast subsidiary. As of October 27, 2018, Procoplast holds short-term debt totaling \$3.0 million, with a weighted average interest rate of 1.75%. As of October 27, 2018, Procoplast holds long-term debt that consists of seventeen notes totaling \$16.8 million, with a weighted-average interest rate of 1.48% and maturities ranging from 2019 to 2031.

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

Cautionary Statement

Certain statements in this report are forward-looking statements that are subject to certain risks and uncertainties. We undertake no duty to update any such forward-looking statements to conform to actual results or changes in our expectations. Our business is highly dependent upon two large automotive customers and specific makes and models of vehicles. Our results will be subject to many of the same risks that apply to the automotive, appliance, computer and communications industries, such as general economic conditions, interest rate fluctuations, consumer spending patterns and technological changes. Other factors which may result in materially different results for future periods include the following risk factors. Additional risks and uncertainties not presently known or that our management currently believe to be insignificant may also adversely affect our financial condition or results of operations. These risk factors should be considered in connection with evaluating the forward-looking statements contained in this report because these factors could cause our actual results and condition to differ materially from those projected in forward-looking statements. The forward-looking statements in this report are subject to the safe harbor protection provided under the securities laws and are made as of the date of this report. Among the factors that could cause actual results to differ materially from past results and future plans and projected future results are the following:

Our business is highly dependent on two large automotive customers. If we were to lose either of these customers or experienced a significant decline in the volume or price of products purchased by these customers, or if either of the customers declared bankruptcy, our future results could be adversely affected.

Because we derive a substantial portion of our revenues from customers in the automotive, appliance, computer, communications and commercial vehicle industries, we are susceptible to trends and factors affecting those industries. International trade disputes could result in tariffs and other protectionist measures that could adversely affect the Company's business.

Our ability to market our automotive products is subject to a lengthy sales cycle, which requires significant investment prior to significant sales revenues, and there is no assurance that our products will be implemented in any particular vehicle.

Our inability to effectively manage the timing, volume, quality and cost of new program launches could adversely affect our financial performance.

Any changes in U.S. trade policy could trigger retaliatory actions by affected countries, resulting in 'trade wars.'

We are subject to continuing pressure to lower our prices.

Our Dabir Surface medical device products are emerging technologies. Our ability to successfully market and sell these products, and the timing of such sales, will depend on acceptance by the medical community and other potential

customers.

▲ significant fluctuation between the U.S. dollar and other currencies could adversely impact our operating results.

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A significant portion of our business activities are conducted in foreign countries, exposing us to additional risks that may not exist in the United States.

We may be required to recognize additional impairment charges on assets, such as goodwill, intangible assets and property, plant and equipment, which could be material to our financial statements.

We are dependent on the availability and price of materials.

Our gross margins are subject to fluctuations due to many factors such as geographical and vertical market pricing mix, pricing reductions and various manufacturing cost variables.

Should a catastrophic event or other significant business interruption occur at any of our facilities, we could face significant reconstruction or remediation costs, penalties, third party liability and loss of production capacity, which could adversely affect our business.

Any decision to strategically divest one or more current businesses or our inability to capitalize on prior or future acquisitions may adversely affect our business.

Disruption of our supply chain could have an adverse effect on our business, financial condition and results of operations.

Changes in our effective tax rate may harm our results of operations.

We may be unable to keep pace with rapid technological changes, which could adversely affect our business.

The Company is exposed to, and may be adversely affected by, potential security breaches or other disruptions to its information technology systems and data security.

Products we manufacture may contain design or manufacturing defects that could result in reduced demand for our products or services, costs associated with recalls, or liability claims against us.

Our technology-based businesses and the markets in which we operate are highly competitive. If we are unable to compete effectively, our sales could decline.

If we are unable to protect our intellectual property or we infringe, or are alleged to infringe, on another person's intellectual property, our business, financial condition and operating results could be materially adversely affected.

We cannot guarantee that the Grakon, Pacific Insight and Procoplast businesses will be successful or that we can implement and profit from any new applications of the acquired technology.

Our long-term incentive plan could require significant adjustments to compensation expense in our condensed consolidated statements of operations if management changes its determinations on the probability of meeting certain performance levels. The adjustments could be material to the financial statements.

Regulations related to the use of conflict-free minerals may increase our costs and expenses, and an inability to certify that our products are conflict-free may adversely affect customer relationships.

Any such forward-looking statements are not guarantees of future performance and actual results, developments and business decisions may differ materially from those foreseen in such forward-looking statements. These forward-looking statements speak only as of the date of the report, press release, statement, document, webcast or oral discussion in which they are made. We do not intend to update any forward-looking statements, all of which are expressly qualified by the foregoing. See Part I — Item 1A, Risk Factors of our Form 10-K for the fiscal year ended April 28, 2018 and Part II — Item 1A, Risk Factors of this Form 10-Q for further discussions regarding some of the reasons that actual results may be materially different from those we anticipate.

### Overview

We are a global manufacturer of component and subsystem devices with manufacturing, design and testing facilities in Belgium, Canada, China, Egypt, Germany, India, Italy, Lebanon, Malta, Mexico, the Netherlands, Singapore, Switzerland, the United Kingdom and the United States. Our primary manufacturing facilities are located in Shanghai and Dongguan, China; Cairo, Egypt; Mriehel, Malta; Monterrey and Fresnillo, Mexico; and Nelson, British Columbia, Canada. We design, manufacture and market devices employing electrical, radio remote control, electronic, wireless, sensing and optical



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technologies. Our business is managed on a segment basis, with those segments being Automotive, Industrial, Medical and Interface. For more information regarding the business and products of these segments, see “Item 1. Business.” of our Form 10-K for the fiscal year ended April 28, 2018, and the descriptions below regarding the business and products of our Grakon subsidiary, which was acquired in September 2018.

Our components are found in the primary end-markets of the aerospace, appliance, automotive, construction, consumer and industrial equipment, communications (including information processing and storage, networking equipment and wireless and terrestrial voice/data systems), medical, rail and other transportation industries.

Recent Events

On September 12, 2018, we acquired 100% of the stock of Grakon for \$421.6 million in cash, net of cash acquired. The business, headquartered in Seattle, Washington, is a manufacturer of custom designed lighting solutions and highly styled engineered components. Grakon’s manufacturing capabilities and products will help diversify our product offerings and expand the Industrial segment, which is a key component of our strategic direction. The accounts and transactions of Grakon have been included in the Automotive and Industrial segments in the consolidated financial statements from the effective date of the acquisition. For goodwill impairment testing purposes, Grakon has been included in the Company's North American Auto and Industrial reporting units.

In connection with the agreement to purchase Grakon, on September 12, 2018, the Company amended its Credit Agreement. The Credit Agreement now has a maturity date of September 12, 2023. The Credit Agreement includes a senior unsecured revolving credit facility and a senior unsecured term loan, which are guaranteed by the Company’s wholly-owned U.S. subsidiaries.

Effective October 27, 2018, the Company reorganized the reportable segments within its business to align to its new structure resulting from the acquisition of Grakon. Prior to this reorganization, the Company's four reportable segments were Automotive, Power, Interface and Other. As a result of this change, the Company's four reportable segments are now Automotive, Industrial, Interface and Medical. Historical information has been revised to reflect the new reportable segments.

In the first quarter of fiscal 2018, we acquired 100% of the stock of Procoplast for \$22.2 million in cash, net of cash acquired. The business, located near the Belgian-German border, is an independent manufacturer of automotive assemblies. The accounts and transactions of Procoplast have been included in the Automotive segment in the consolidated financial statements from the effective date of the acquisition.

In the second quarter of fiscal 2018, Methode acquired 100% of the outstanding common shares of Pacific Insight in a cash transaction for \$107.7 million, net of cash acquired. Pacific Insight, headquartered in Vancouver, British Columbia, Canada, is a global solutions provider offering design, development, manufacturing and delivery of lighting and electronic products and full-service solutions to the automotive and commercial vehicle markets. Its technology in LED-based ambient and direct lighting will expand our presence within the automotive interior, as well as augment our efforts in overhead console and other areas. The accounts and transactions of Pacific Insight have been included in the Automotive segment in the consolidated financial statements from the effective date of the acquisition.

Hetronic Germany-GmbH Matters

For several years, Hetronic Germany-GmbH and Hydronic-Steuersysteme-GmbH (the “Fuchs companies”) served as our distributors for Germany, Austria and other central and eastern European countries pursuant to their respective intellectual property licenses and distribution and assembly agreements. We became aware that the Fuchs companies and their managing director, Albert Fuchs, had materially violated those agreements. As a result, we terminated all of our agreements with the Fuchs companies. On June 20, 2014, we filed a lawsuit against the Fuchs companies in the Federal District Court for the Western District of Oklahoma alleging material breaches of the distribution and assembly agreements seeking damages, as well as various forms of injunctive relief. The defendants have filed

counterclaims alleging breach of contract, interference with business relations and business slander. On April 2, 2015, we amended our complaint against the Fuchs companies to add additional unfair competition and Lanham Act claims and to add additional affiliated parties. As of October 27, 2018, the matter remains in the pre-trial stage.

We incurred Hetronic-related legal fees of \$1.0 million and \$1.6 million during the three months ended October 27, 2018 and October 28, 2017, respectively. For the six months ended October 27, 2018 and October 28, 2017, we incurred Hetronic-related legal fees of \$1.9 million and \$4.5 million, respectively.

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Results of Operations for the Three Months Ended October 27, 2018 as Compared to the Three Months Ended October 28, 2017

Consolidated Results

Below is a table summarizing results for the three months ended:

| (Dollars in Millions)               | October 27,<br>2018 | October 28,<br>2017 | Net Change<br>(\$) | Net Change<br>(%) |   |
|-------------------------------------|---------------------|---------------------|--------------------|-------------------|---|
| Net Sales                           | \$ 264.0            | \$ 230.1            | \$ 33.9            | 14.7              | % |
| Cost of Products Sold               | 193.2               | 168.1               | 25.1               | 14.9              | % |
| Gross Profit                        | 70.8                | 62.0                | 8.8                | 14.2              | % |
| Selling and Administrative Expenses | 48.0                | 31.2                | 16.8               | 53.8              | % |
| Amortization of Intangibles         | 3.7                 | 1.1                 | 2.6                | 236.4             | % |
| Interest Expense, Net               | 1.6                 | 0.2                 | 1.4                | N/M               | * |
| Other Expense (Income), Net         | (0.1 )              | 0.4                 | (0.5 )             | N/M               | * |
| Income Tax Expense                  | 3.0                 | 4.9                 | (1.9 )             | (38.8 )           | % |
| Net Income                          | \$ 14.6             | \$ 24.2             | \$ (9.6 )          | (39.7 )           | % |
| Percent of sales:                   | October 27,<br>2018 | October 28,<br>2017 |                    |                   |   |
| Net Sales                           | 100.0               | % 100.0             | %                  |                   |   |
| Cost of Products Sold               | 73.2                | % 73.1              | %                  |                   |   |
| Gross Margins                       | 26.8                | % 26.9              | %                  |                   |   |
| Selling and Administrative Expenses | 18.2                | % 13.6              | %                  |                   |   |
| Amortization of Intangibles         | 1.4                 | % 0.5               | %                  |                   |   |
| Interest Expense, Net               | 0.6                 | % 0.1               | %                  |                   |   |
| Other Expense (Income), Net         | —                   | % 0.2               | %                  |                   |   |
| Income Tax Expense                  | 1.1                 | % 2.1               | %                  |                   |   |
| Net Income                          | 5.5                 | % 10.5              | %                  |                   |   |

\* N/M equals non-meaningful

Net Sales. Consolidated net sales increased \$33.9 million, or 14.7%, to \$264.0 million for the three months ended October 27, 2018, from \$230.1 million for the three months ended October 28, 2017. The Automotive segment net sales increased \$14.9 million, or 8.0%, to \$201.6 million for the second quarter of fiscal 2019, from \$186.7 million for the second quarter of fiscal 2018. The Industrial segment net sales increased \$22.7 million, or 91.9%, to \$47.4 million for the second quarter of fiscal 2019, from \$24.7 million for the second quarter of fiscal 2018. The Interface segment net sales decreased \$4.0 million, or 21.4%, to \$14.7 million for the second quarter of fiscal 2019, compared to \$18.7 million for the second quarter of fiscal 2018. The Medical segment net sales increased to \$0.3 million for the second quarter of fiscal 2019, compared to no net sales for the second quarter of fiscal 2018. Translation of foreign operations' net sales for the three months ended October 27, 2018 decreased reported net sales by \$1.6 million, or 0.6%, due to average currency rate fluctuations in the second quarter of fiscal 2019, compared to the second quarter of fiscal 2018, primarily due to the weakening of the euro and Chinese yuan as compared to the U.S. dollar.

Cost of Products Sold. Consolidated cost of products sold increased \$25.1 million, or 14.9%, to \$193.2 million for the three months ended October 27, 2018, compared to \$168.1 million for the three months ended October 28, 2017. Consolidated cost of products sold as a percentage of net sales was 73.2% for the second quarter of fiscal 2019, compared to 73.1% for the second quarter of fiscal 2018. The Automotive segment cost of products sold as a percentage of net sales increased primarily due to sales mix related to our Pacific Insight business, which currently has a higher cost of products sold as a percentage of sales compared to other reporting units within the Automotive

segment. In addition, the results of the second quarter of fiscal 2018, included only one month of Pacific Insight's results. The cost of products sold as a percentage of net sales also increased due to pricing reductions on certain products, partially offset by the weakening of the Mexican peso as compared to the U.S.

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dollar during the period. The Industrial segment cost of products sold as a percentage of net sales decreased in the second quarter of fiscal 2019 due primarily to a favorable sales mix relating to our Grakon business and increased sales volumes of busbar and radio remote control products. In addition, the second quarter of fiscal 2019 includes \$2.6 million of purchase accounting related adjustments related to the Grakon acquisition. The Interface segment cost of products sold as a percentage of net sales increased primarily due to lower sales volumes of our appliance products and lower sales volumes and unfavorable sales mix of our data solutions products, partially offset by the weakening of the Mexican peso as compared to the U.S. dollar during the period. The Medical segment cost of products sold increased primarily due to an increase in sales volumes during the period.

**Gross Profit.** Consolidated gross profit increased \$8.8 million, or 14.2%, to \$70.8 million for the three months ended October 27, 2018, as compared to \$62.0 million for the three months ended October 28, 2017. Gross margins as a percentage of net sales decreased slightly to 26.8% for the three months ended October 27, 2018, compared to 26.9% for the three months ended October 28, 2017. The Automotive segment gross margins as a percentage of net sales decreased due primarily to sales mix related to our Pacific Insight business, which currently has a higher cost of products sold as a percentage of sales compared to other reporting units within the Automotive segment. In addition, the results of the second quarter of fiscal 2018, included only one month of Pacific Insight's results. The cost of products sold as a percentage of net sales also increased due to pricing reductions on certain products, partially offset by the weakening of the Mexican peso as compared to the U.S. dollar during the period. The Industrial segment gross margins increased due primarily to a favorable sales mix relating to our Grakon business and increased sales volumes of busbar and radio remote control products. In addition, the second quarter of fiscal 2019 includes \$2.6 million of purchase accounting related adjustments related to the Grakon acquisition. The Interface segment gross profit as a percentage of net sales decreased due primarily to lower sales volumes of our appliance products and lower sales volumes and unfavorable sales mix of our data solutions products, partially offset by the weakening of the Mexican peso as compared to the U.S. dollar during the period. The Medical segment gross margins improved primarily due to an increase in sales volumes during the period.

**Selling and Administrative Expenses.** Selling and administrative expenses increased by \$16.8 million, or 53.8%, to \$48.0 million for the three months ended October 27, 2018, compared to \$31.2 million for the three months ended October 28, 2017. Selling and administrative expenses as a percentage of net sales increased to 18.2% for the three months ended October 27, 2018 from 13.6% for the three months ended October 28, 2017. The increase in selling and administrative expenses is partially attributable to the Grakon and Pacific Insight businesses, which were not owned by Methode during the entirety of the three months ended October 28, 2017, which accounted for \$7.3 million of the increase. Excluding the activity from our Grakon and Pacific Insight businesses, expenses increased \$9.5 million due primarily to a \$5.7 million increase in stock award amortization expense and higher acquisition-related costs of \$4.9 million, partially offset by lower legal fees of \$1.1 million.

**Amortization of Intangibles.** Amortization of intangibles increased \$2.6 million, or 236.4%, to \$3.7 million for the three months ended October 27, 2018, compared to \$1.1 million for the three months ended October 28, 2017. The increase is due to the amortization expense related to our Grakon and Pacific Insight businesses.

**Interest Expense, Net.** Interest expense, net was \$1.6 million for the three months ended October 27, 2018, as compared to \$0.2 million for the three months ended October 28, 2017. The increase in expense primarily relates to increased debt levels in the second quarter of fiscal 2019, compared to the second quarter of fiscal 2018.

**Other Expense (Income), Net.** Other expense (income), net was income of \$0.1 million for the three months ended October 27, 2018, as compared to expense of \$0.4 million for the three months ended October 28, 2017. All amounts for both the second quarter of fiscal 2019 and the second quarter of fiscal 2018 relate to currency rate fluctuations. The functional currencies of our operations are the British pound, Canadian dollar, Chinese yuan, euro, Hong Kong dollar, Indian rupee, Mexican peso, Singapore dollar, Swiss franc and U.S. dollar. Some foreign operations have transactions denominated in currencies other than their functional currencies, primarily sales in U.S. dollars, euros and Chinese yuan, creating exchange rate sensitivities.

**Income Tax Expense.** Income tax expense decreased \$1.9 million, or 38.8%, to \$3.0 million for the three months ended October 27, 2018, compared to \$4.9 million for the three months ended October 28, 2017. The Company's effective tax rate increased slightly to 17.0% in the second quarter of fiscal 2019, compared to 16.8% in the second

quarter of fiscal 2018. The increase primarily relates to a favorable one-time effect from a state income tax rate change in the second quarter of fiscal 2018.

Net Income. Net income was \$14.6 million for the three months ended October 27, 2018, compared to \$24.2 million for the three months ended October 28, 2017. Net income decreased due primarily to higher stock award amortization expense, higher acquisition-related expenses, higher amortization of intangible assets and increased interest expense, partially offset by

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increased sales volumes and net income from our recent acquisitions, lower legal fees, higher sales of our busbar and radio remote control products and the weakening of the Mexican peso as compared to the U.S. dollar during the period.

## Operating Segments

## Automotive Segment Results

Below is a table summarizing results for the three months ended:

| (Dollars in Millions)               | October 27, 2018 |  | October 28, 2017 |  | Net Change |          |
|-------------------------------------|------------------|--|------------------|--|------------|----------|
|                                     |                  |  |                  |  | (\$)       | (%)      |
| Net Sales                           | \$ 201.6         |  | \$ 186.7         |  | \$ 14.9    | 8.0 %    |
| Cost of Products Sold               | 146.7            |  | 133.9            |  | 12.8       | 9.6 %    |
| Gross Profit                        | 54.9             |  | 52.8             |  | 2.1        | 4.0 %    |
| Selling and Administrative Expenses | 16.3             |  | 9.4              |  | 6.9        | 73.4 %   |
| Amortization of Intangibles         | 1.8              |  | 0.5              |  | 1.3        | 260.0 %  |
| Income from Operations              | \$ 36.8          |  | \$ 42.9          |  | \$ (6.1 )  | (14.2 )% |

| Percent of sales:                   | October 27, 2018 |   | October 28, 2017 |   |
|-------------------------------------|------------------|---|------------------|---|
|                                     |                  | % |                  | % |
| Net Sales                           | 100.0            | % | 100.0            | % |
| Cost of Products Sold               | 72.8             | % | 71.7             | % |
| Gross Margins                       | 27.2             | % | 28.3             | % |
| Selling and Administrative Expenses | 8.1              | % | 5.0              | % |
| Amortization of Intangibles         | 0.9              | % | 0.3              | % |
| Income from Operations              | 18.3             | % | 23.0             | % |

Net Sales. Automotive segment net sales increased \$14.9 million, or 8.0%, to \$201.6 million for the three months ended October 27, 2018, from \$186.7 million for the three months ended October 28, 2017. Net sales increased in North America by \$24.0 million, or 23.1%, to \$127.8 million in the second quarter of fiscal 2019, compared to \$103.8 million in the second quarter of fiscal 2018. North American automotive sales in the second quarter of fiscal 2019 include \$6.1 million from Grakon, which was acquired in the second quarter of fiscal 2019, and \$24.4 million from Pacific Insight, which was acquired in the second quarter of fiscal 2018. The second quarter of fiscal 2019 included approximately six weeks of Grakon's results. The second quarter of fiscal 2018 included only one month of Pacific Insight's results, which included \$6.9 million of net sales. Other North American sales increased for our integrated center stack products due primarily to higher sales volumes, partially offset by pricing reductions. Sales for our transmission lead-frame assemblies decreased due primarily to pricing reductions and lower sales volumes in the second quarter of fiscal 2019, compared to the second quarter of fiscal 2018. Sales of our human machine interface assembly products increased primarily due to increased sales volumes as the result of new program launches. Net sales in Europe decreased \$7.3 million, or 12.5%, to \$51.3 million in the second quarter of fiscal 2019, compared to \$58.6 million in the second quarter of fiscal 2018. European sales decreased primarily due to the exclusion of pre-production reimbursements from net sales due to the adoption of ASC 606 on April 29, 2018, partially offset by higher sales volumes of sensor products. European pre-production reimbursements were \$6.2 million during the three months ended October 28, 2017. Net sales in Asia decreased \$1.8 million, or 7.4%, to \$22.5 million in the second quarter of fiscal 2019, compared to \$24.3 million in the second quarter of fiscal 2018, primarily due to lower sales of our transmission lead-frame assemblies due to a combination of pricing reductions and lower sales volumes. In addition, sales volumes for steering angle sensor products were lower, as the products approach end of production. Translation of foreign operations' net sales for the three months ended October 27, 2018 decreased reported net sales by \$1.6 million, or 0.8%, due to average currency rates in the second quarter of fiscal 2019, compared to the average

currency rates in the second quarter of fiscal 2018, primarily due to the weakening of the euro and Chinese yuan as compared to the U.S. dollar.

Cost of Products Sold. Automotive segment cost of products sold increased \$12.8 million, or 9.6%, to \$146.7 million for the three months ended October 27, 2018, compared to \$133.9 million for the three months ended October 28, 2017. The Automotive segment cost of products sold as a percentage of net sales increased to 72.8% in the second quarter of fiscal 2019,



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compared to 71.7% in the second quarter of fiscal 2018. The cost of products sold as a percentage of net sales increased primarily due to sales mix related to our Pacific Insight business, which currently has a higher cost of products sold as a percentage of sales compared to other reporting units within the Automotive segment. In addition, the results of the second quarter of fiscal 2018, included only one month of Pacific Insight's results. The cost of products sold as a percentage of net sales also increased due to pricing reductions on certain products, partially offset by the weakening of the Mexican peso as compared to the U.S. dollar during the period.

**Gross Profit.** Automotive segment gross profit increased \$2.1 million, or 4.0%, to \$54.9 million for the three months ended October 27, 2018, as compared to \$52.8 million for the three months ended October 28, 2017. The Automotive segment gross margins as a percentage of net sales decreased to 27.2% for the three months ended October 27, 2018, as compared to 28.3% for the three months ended October 28, 2017. Gross margins as a percentage of net sales decreased due primarily to sales mix related to our Pacific Insight business, which currently has a higher cost of products sold as a percentage of sales compared to other reporting units within the Automotive segment. In addition, the results of the second quarter of fiscal 2018, included only one month of Pacific Insight's results. The cost of products sold as a percentage of net sales also increased due to pricing reductions on certain products, partially offset by the weakening of the Mexican peso as compared to the U.S. dollar during the period.

**Selling and Administrative Expenses.** Selling and administrative expenses increased \$6.9 million, or 73.4%, to \$16.3 million for the three months ended October 27, 2018, as compared to \$9.4 million for the three months ended October 28, 2017. Selling and administrative expenses as a percentage of net sales increased to 8.1% for the three months ended October 27, 2018, from 5.0% for the three months ended October 28, 2017. The increase in selling and administrative expenses is partially attributable to the Pacific Insight and Grakon businesses, which were not owned by Methode during the entirety of the three months ended October 28, 2017. This accounted for \$1.6 million of the increase. Excluding the activity from our Pacific Insight and Grakon businesses, expenses increased \$5.3 million due primarily to the increase in stock award amortization expense for our long-term incentive program. The second quarter of fiscal 2018 also includes a benefit of \$1.1 million due to acquisition costs that were reclassified out of the Automotive segment and into the corporate segment during the period.

**Amortization of Intangibles.** Amortization of intangibles increased \$1.3 million, or 260.0%, to \$1.8 million for the three months ended October 27, 2018, as compared to \$0.5 million for the three months ended October 28, 2017.

Amortization of intangibles as a percentage of net sales increased to 0.9% for the three months ended October 27, 2018, from 0.3% for the three months ended October 28, 2017.

**Income from Operations.** Automotive segment income from operations decreased \$6.1 million, or 14.2%, to \$36.8 million for the three months ended October 27, 2018, compared to \$42.9 million for the three months ended October 28, 2017. Income from operations for the second quarter of fiscal 2019 decreased due primarily to increased stock award amortization expense, pricing reductions on certain products and increased intangible asset amortization expense, partially offset by the income from operations from our Grakon and Pacific Insight businesses and the weakening of the Mexican peso as compared to the U.S. dollar during the period.

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## Industrial Segment Results

Below is a table summarizing results for the three months ended:

| (Dollars in Millions)               | October 27,<br>2018 | October 28,<br>2017 | Net Change<br>(\$) | Net Change<br>(%) |   |
|-------------------------------------|---------------------|---------------------|--------------------|-------------------|---|
| Net Sales                           | \$ 47.4             | \$ 24.7             | \$ 22.7            | 91.9              | % |
| Cost of Products Sold               | 33.2                | 18.3                | 14.9               | 81.4              | % |
| Gross Profit                        | 14.2                | 6.4                 | 7.8                | 121.9             | % |
| Selling and Administrative Expenses | 7.7                 | 3.7                 | 4.0                | 108.1             | % |
| Amortization of Intangibles         | 1.4                 | —                   | 1.4                | —                 | % |
| Income from Operations              | \$ 5.1              | \$ 2.7              | \$ 2.4             | 88.9              | % |

| Percent of sales:                   | October 27,<br>2018 | October 28,<br>2017 |   |  |
|-------------------------------------|---------------------|---------------------|---|--|
| Net Sales                           | 100.0               | % 100.0             | % |  |
| Cost of Products Sold               | 70.0                | % 74.1              | % |  |
| Gross Margins                       | 30.0                | % 25.9              | % |  |
| Selling and Administrative Expenses | 16.2                | % 15.0              | % |  |
| Amortization of Intangibles         | 3.0                 | % —                 | % |  |
| Income from Operations              | 10.8                | % 10.9              | % |  |

**Net Sales.** Industrial segment net sales increased \$22.7 million, or 91.9%, to \$47.4 million for the three months ended October 27, 2018, from \$24.7 million for the three months ended October 28, 2017. Net sales increased in North America by \$18.4 million, or 204.4%, to \$27.4 million in the second quarter of fiscal 2019, compared to \$9.0 million in the second quarter of fiscal 2018. Net sales in North America includes \$18.1 million from Grakon and represents approximately six weeks of results. Excluding the acquisition of Grakon, North American sales increased by \$0.3 million primarily due to increased sales volumes of busbar products in the quarter. Net sales increased in Europe by \$1.1 million, or 11.2%, to \$10.9 million in the second quarter of fiscal 2019, compared to \$9.8 million in the second quarter of fiscal 2018. The increase was due primarily to an increase in sales of radio remote control products, partially offset by a decrease in sales of bypass switches. Net sales in Asia increased \$3.2 million, or 54.2%, to \$9.1 million in the second quarter of fiscal 2019, compared to \$5.9 million in the second quarter of fiscal 2018, primarily due to higher sales volumes of busbar products.

**Cost of Products Sold.** Industrial segment cost of products sold increased \$14.9 million, or 81.4%, to \$33.2 million for the three months ended October 27, 2018, compared to \$18.3 million for the three months ended October 28, 2017. Industrial segment cost of products sold as a percentage of net sales decreased to 70.0% for the three months ended October 27, 2018, compared to 74.1% for the three months ended October 28, 2017. Cost of products sold as a percentage of net sales decreased in the second quarter of fiscal 2019 due primarily to a favorable sales mix relating to our Grakon business and increased sales volumes of busbar and radio remote control products. In addition, the second quarter of fiscal 2019 includes \$2.6 million of purchase accounting related adjustments related to the Grakon acquisition.

**Gross Profit.** Industrial segment gross profit increased \$7.8 million, or 121.9%, to \$14.2 million for the three months ended October 27, 2018, compared to \$6.4 million for the three months ended October 28, 2017. Gross margins as a percentage of net sales increased to 30.0% for the three months ended October 27, 2018, compared to 25.9% for the three months ended October 28, 2017. Gross margins increased in the second quarter of fiscal 2019 due primarily to a favorable sales mix relating to our Grakon business and increased sales volumes of busbar and radio remote control products. In addition, the second quarter of fiscal 2019 includes \$2.6 million of purchase accounting related adjustments related to the Grakon acquisition.

**Selling and Administrative Expenses.** Selling and administrative expenses increased \$4.0 million, or 108.1%, to \$7.7 million for the three months ended October 27, 2018, compared to \$3.7 million for the three months ended October 28, 2017. Selling and administrative expenses as a percentage of net sales increased to 16.2% for the three months ended October 27, 2018, from 15.0% for the three months ended October 28, 2017. The results for the three months ended October 27, 2018

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include \$5.7 million of selling and administrative expenses from Grakon. Excluding the impacts of the Grakon acquisition, selling and administrative expenses decreased \$1.7 million due primarily to lower legal fees, partially offset by higher stock award amortization expense for our long-term incentive program.

Amortization of Intangibles. Amortization of Intangibles increased to \$1.4 million for the three months ended October 27, 2018 due primarily to the acquisition of Grakon in the second quarter of fiscal 2019.

Income from Operations. Industrial segment income from operations increased \$2.4 million, or 88.9%, to \$5.1 million for the three months ended October 27, 2018, compared to \$2.7 million for the three months ended October 28, 2017. Income from operations increased due primarily to the income from operations from our Grakon business, lower legal fees and higher sales of busbar and radio remote control products, partially offset by higher stock award amortization expense and lower sales volumes of bypass switches.

## Interface Segment Results

Below is a table summarizing results for the three months ended:

| (Dollars in Millions)               | October 27,<br>2018 | October 28,<br>2017 | Net Change<br>(\$) | Net Change<br>(%) |
|-------------------------------------|---------------------|---------------------|--------------------|-------------------|
| Net Sales                           | \$ 14.7             | \$ 18.7             | \$ (4.0 )          | (21.4 )%          |
| Cost of Products Sold               | 13.2                | 14.9                | (1.7 )             | (11.4 )%          |
| Gross Profit                        | 1.5                 | 3.8                 | (2.3 )             | (60.5 )%          |
| Selling and Administrative Expenses | 1.6                 | 1.1                 | 0.5                | 45.5 %            |
| Amortization of Intangibles         | 0.5                 | 0.6                 | (0.1 )             | (16.7 )%          |
| Income (Loss) from Operations       | \$ (0.6 )           | \$ 2.1              | \$ (2.7 )          | (128.6 )%         |

| Percent of sales:                   | October 27,<br>2018 | October 28,<br>2017 |
|-------------------------------------|---------------------|---------------------|
| Net Sales                           | 100.0 %             | 100.0 %             |
| Cost of Products Sold               | 89.8 %              | 79.7 %              |
| Gross Margins                       | 10.2 %              | 20.3 %              |
| Selling and Administrative Expenses | 10.9 %              | 5.9 %               |
| Amortization of Intangibles         | 3.4 %               | 3.2 %               |
| Income (Loss) from Operations       | (4.1 )%             | 11.2 %              |

Net Sales. Interface segment net sales decreased \$4.0 million, or 21.4%, to \$14.7 million for the three months ended October 27, 2018, compared to \$18.7 million for the three months ended October 28, 2017. Net sales decreased in North America by \$4.0 million, or 21.7%, to \$14.4 million in the second quarter of fiscal 2019, compared to \$18.4 million in the second quarter of fiscal 2018, primarily due to lower sales volumes of appliance and data solution products. Net sales in Asia were unchanged at \$0.3 million for both the second quarter of fiscal 2019 and the second quarter of fiscal 2018.

Cost of Products Sold. Interface segment cost of products sold decreased \$1.7 million, or 11.4%, to \$13.2 million for the three months ended October 27, 2018, compared to \$14.9 million for the three months ended October 28, 2017.

The Interface segment cost of products sold as a percentage of net sales increased to 89.8% for the three months ended October 27, 2018, from 79.7% for the three months ended October 28, 2017. The increase primarily relates to lower sales volumes of our appliance products and lower sales volumes and unfavorable sales mix of our data solutions products, partially offset by the weakening of the Mexican peso as compared to the U.S. dollar during the period.

Gross Profit. Interface segment gross profit decreased \$2.3 million, or 60.5%, to \$1.5 million in the second quarter of fiscal 2019, compared to \$3.8 million in the second quarter of fiscal 2018. Gross margins as a percentage of net sales decreased to 10.2% for the three months ended October 27, 2018, from 20.3% for the three months ended October 28, 2017. The decrease primarily relates to lower sales volumes of our appliance products and lower sales volumes and

unfavorable sales

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mix of our data solutions products, partially offset by the weakening of the Mexican peso as compared to the U.S. dollar during the period.

**Selling and Administrative Expenses.** Selling and administrative expenses increased \$0.5 million, or 45.5%, to \$1.6 million for the three months ended October 27, 2018, compared to \$1.1 million for the three months ended October 28, 2017. Selling and administrative expenses as a percentage of net sales increased to 10.9% for the three months ended October 27, 2018, from 5.9% for the three months ended October 28, 2017. During the period, higher stock award amortization expense was partially offset by lower legal expense.

**Amortization of Intangibles.** Amortization of intangibles decreased \$0.1 million, or 16.7%, to \$0.5 million for the three months ended October 27, 2018, compared to \$0.6 million for the three months ended October 28, 2017.

Amortization of intangibles as a percentage of net sales increased to 3.4% for the three months ended October 27, 2018, from 3.2% for the three months ended October 28, 2017.

**Income (Loss) From Operations.** Interface segment income from operations decreased \$2.7 million to a loss of \$0.6 million for the three months ended October 27, 2018, compared to income of \$2.1 million for the three months ended October 28, 2017. Income from operations decreased due primarily to lower sales volumes of our appliance products and lower sales volumes and unfavorable sales mix of our data solutions products, partially offset by a favorable currency impact for appliance products due to the weakening of the Mexican peso as compared to the U.S. dollar.

**Medical Segment Results**

Below is a table summarizing results for the three months ended:

| (Dollars in Millions)               | October 27, October 28, |           | Net Change<br>(\$) | Net Change |     |
|-------------------------------------|-------------------------|-----------|--------------------|------------|-----|
|                                     | 2018                    | 2017      |                    | (%)        | (%) |
| Net Sales                           | \$ 0.3                  | \$ —      | \$ 0.3             | —          | %   |
| Cost of Products Sold               | 1.0                     | 0.9       | 0.1                | 11.1       | %   |
| Gross Profit                        | (0.7 )                  | (0.9 )    | 0.2                | (22.2 )    | %   |
| Selling and Administrative Expenses | 1.8                     | 2.2       | (0.4 )             | (18.2 )    | %   |
| Loss from Operations                | \$ (2.5 )               | \$ (3.1 ) | \$ 0.6             | (19.4 )    | %   |

| Percent of sales:                   | October 27, October 28, |      |
|-------------------------------------|-------------------------|------|
|                                     | 2018                    | 2017 |
| Net Sales                           | 100.0 %                 | — %  |
| Cost of Products Sold               | 333.3 %                 | — %  |
| Gross Margins                       | (233.3 )%               | — %  |
| Selling and Administrative Expenses | 600.0 %                 | — %  |
| Amortization of Intangibles         | — %                     | — %  |
| Loss from Operations                | (833.3 )%               | — %  |

**Net Sales.** The Medical segment had net sales of \$0.3 million in the second quarter of fiscal 2019, compared to minimal net sales in the second quarter of fiscal 2018, due primarily to an expansion in our customer base.

**Cost of Products Sold.** Medical segment cost of products sold was \$1.0 million for the three months ended October 27, 2018, compared to \$0.9 million for the three months ended October 28, 2017. The increase primarily relates to an increase in sales volumes during the period.

**Gross Profit.** The Medical segment gross profit was a loss of \$0.7 million for the three months ended October 27, 2018, compared to a loss of \$0.9 million for the three months ended October 28, 2017. The decreased loss primarily relates to an increase in sales volumes during the period.

**Selling and Administrative Expenses.** Selling and administrative expenses decreased \$0.4 million, to \$1.8 million for the three months ended October 27, 2018, compared to \$2.2 million for the three months ended October 28, 2017. The



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decrease in selling and administrative expenses for the second quarter of fiscal 2019 primarily relates to decreased marketing expense, partially offset by increased salary and bonus expense in the period.

Loss From Operations The Medical segment loss from operations decreased \$0.6 million, to \$2.5 million for the three months ended October 27, 2018, compared to \$3.1 million for the three months ended October 28, 2017. The decreased loss relates to higher sales volumes and decreased marketing expense in the period, partially offset by increased salary and bonus expense during the period.

Results of Operations for the Six Months Ended October 27, 2018 as Compared to the Six Months Ended October 28, 2017

## Consolidated Results

Below is a table summarizing results for the six months ended:

| (Dollars in Millions)               | October 27, October 28, |          | Net Change |        | Net Change |
|-------------------------------------|-------------------------|----------|------------|--------|------------|
|                                     | 2018                    | 2017     | (\$)       | (%)    |            |
| Net Sales                           | \$ 487.4                | \$ 431.3 | \$ 56.1    | 13.0   | %          |
| Cost of Products Sold               | 356.5                   | 313.7    | 42.8       | 13.6   | %          |
| Gross Profit                        | 130.9                   | 117.6    | 13.3       | 11.3   | %          |
| Selling and Administrative Expenses | 77.5                    | 60.8     | 16.7       | 27.5   | %          |
| Amortization of Intangibles         | 5.6                     | 1.7      | 3.9        | 229.4  | %          |
| Interest Expense, Net               | 1.8                     | —        | 1.8        | N/M    | *          |
| Other Expense, Net                  | 0.2                     | 1.2      | (1.0)      | N/M    | *          |
| Income Tax Expense                  | 7.5                     | 9.2      | (1.7)      | (18.5) | %          |
| Net Income                          | \$ 38.3                 | \$ 44.7  | \$ (6.4)   | (14.3) | %          |

| Percent of sales:                   | October 27, October 28, |         |   |  |
|-------------------------------------|-------------------------|---------|---|--|
|                                     | 2018                    | 2017    |   |  |
| Net Sales                           | 100.0                   | % 100.0 | % |  |
| Cost of Products Sold               | 73.1                    | % 72.7  | % |  |
| Gross Margins                       | 26.9                    | % 27.3  | % |  |
| Selling and Administrative Expenses | 15.9                    | % 14.1  | % |  |
| Amortization of Intangibles         | 1.1                     | % 0.4   | % |  |
| Interest Expense, Net               | 0.4                     | % —     | % |  |
| Other Expense, Net                  | —                       | % 0.3   | % |  |
| Income Tax Expense                  | 1.5                     | % 2.1   | % |  |
| Net Income                          | 7.9                     | % 10.4  | % |  |

\* N/M equals non-meaningful

Net Sales. Consolidated net sales increased by \$56.1 million, or 13.0%, to \$487.4 million for the six months ended October 27, 2018, from \$431.3 million for the six months ended October 28, 2017. The Automotive segment net sales increased \$33.7 million, or 9.8%, to \$376.9 million for the six months ended October 27, 2018, from \$343.2 million for the six months ended October 28, 2017. The Industrial segment net sales increased \$29.1 million, or 57.6%, to \$79.6 million for the six months ended October 27, 2018, from \$50.5 million for the six months ended October 28, 2017. The Interface segment net sales decreased \$7.2 million, or 19.2%, to \$30.3 million for the six months ended October 27, 2018, compared to \$37.5 million for the six months ended October 28, 2017. The Medical segment net sales increased \$0.5 million to \$0.6 million for the six months ended October 27, 2018, compared to \$0.1 million for the six months ended October 28, 2017. Translation of foreign operations' net sales for the six months ended October 27, 2018 increased net sales by \$1.1 million, or 0.2%, compared to the average currency rates in the six months ended October 28, 2017, primarily due to the strengthening of the euro and Chinese yuan as compared to the



U.S. dollar.

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**Cost of Products Sold.** Consolidated cost of products sold increased \$42.8 million, or 13.6%, to \$356.5 million for the six months ended October 27, 2018, compared to \$313.7 million for the six months ended October 28, 2017.

Consolidated cost of products sold as a percentage of net sales increased to 73.1% for the six months ended October 27, 2018, compared to 72.7% for the six months ended October 28, 2017. The Automotive segment cost of products sold as a percentage of net sales increased primarily due to sales mix related to our Pacific Insight business, which currently has a higher costs of products sold as a percentage of sales compared to other reporting units within the Automotive segment. In addition, the results of the second half of fiscal 2018, included only one month of Pacific Insight's results. The cost of products sold as a percentage of net sales also increased due to pricing reductions on certain products, partially offset by the weakening of the Mexican peso as compared to the U.S. dollar during the period. The Industrial segment cost of products sold as a percentage of net sales decreased primarily due to a favorable sales mix relating to our Grakon business and increased sales volumes of radio remote control and busbar products. In addition, the first half of fiscal 2019 includes \$2.6 million of purchase accounting related adjustments related to the Grakon acquisition. The Interface segment cost of products sold as a percentage of net sales increased primarily due to lower sales volumes of our appliance products and lower sales volumes and unfavorable sales mix of our data solutions products, partially offset by the weakening of the Mexican peso as compared to the U.S. dollar during the period. The Medical segment cost of products sold increased primarily due to an increase in sales volumes during the period.

**Gross Profit.** Consolidated gross profit increased \$13.3 million, or 11.3%, to \$130.9 million for the six months ended October 27, 2018, as compared to \$117.6 million for the six months ended October 28, 2017. Gross margins as a percentage of net sales decreased to 26.9% for six months ended October 27, 2018, compared to 27.3% for the six months ended October 28, 2017. The Automotive segment gross margins as a percentage of net sales decreased due primarily to sales mix related to our Pacific Insight business, which currently has a higher costs of products sold as a percentage of sales compared to other reporting units within the Automotive segment. In addition, the results of the first half of fiscal 2018, included only one month of Pacific Insight's results. The cost of products sold as a percentage of net sales also increased due to pricing reductions on certain products, partially offset by the weakening of the Mexican peso as compared to the U.S. dollar during the period. The Industrial segment gross margins increased due primarily to a favorable sales mix relating to our Grakon business and increased sales volumes of radio remote control and busbar products. In addition, the first half of fiscal 2019 includes \$2.6 million of purchase accounting related adjustments related to the Grakon acquisition. The Interface segment gross margins as a percentage of sales decreased primarily due to lower sales volumes of our appliance products and lower sales volumes and unfavorable sales mix of our data solutions products, partially offset by the weakening of the Mexican peso as compared to the U.S. dollar during the period. The Medical segment gross profit increased due primarily to an increase in sales volumes during the period.

**Selling and Administrative Expenses.** Selling and administrative expenses increased \$16.7 million, or 27.5%, to \$77.5 million for the six months ended October 27, 2018, compared to \$60.8 million for the six months ended October 28, 2017. Selling and administrative expenses as a percentage of net sales increased to 15.9% for the six months ended October 27, 2018 from 14.1% for the six months ended October 28, 2017. The increase in selling and administrative expenses is partially attributable to the Grakon, Pacific Insight and Procoplast businesses, which were not owned by Methode during the entirety of the six months ended October 28, 2017. This accounted for \$11.0 million of the increase. Excluding the activity from our Grakon, Pacific Insight and Procoplast businesses, expenses increased \$5.7 million due primarily to a \$3.7 million increase in stock award amortization expense, higher acquisition-related costs of \$2.9 million and higher salary and other personnel costs, partially offset by lower legal fees of \$2.8 million.

**Amortization of Intangibles.** Amortization of intangibles increased \$3.9 million, or 229.4%, to \$5.6 million for the six months ended October 27, 2018, compared to \$1.7 million for the six months ended October 28, 2017. The increase is primarily due to the amortization expense related to our Grakon and Pacific Insight businesses.

**Interest Expense, Net.** Interest expense, net was \$1.8 million for the six months ended October 27, 2018, compared to zero for the six months ended October 28, 2017. This change is due to the increased debt levels during the period.

**Other Expense, Net.** Other expense, net decreased \$1.0 million to \$0.2 million for the six months ended October 27, 2018, compared to \$1.2 million for the six months ended October 28, 2017. All amounts for both the six months

ended October 27, 2018 and the six months ended October 28, 2017 relate to currency rate fluctuations. The functional currencies of our operations are the British pound, Canadian dollar, Chinese yuan, euro, Hong Kong dollar, Indian rupee, Mexican peso, Singapore dollar, Swiss franc and U.S. dollar. Some foreign operations have transactions denominated in currencies other than their functional currencies, primarily sales in U.S. dollars, euros and Chinese yuan, creating exchange rate sensitivities.

**Income Tax Expense.** Income tax expense decreased \$1.7 million, or 18.5%, to \$7.5 million for the six months ended October 27, 2018, compared to \$9.2 million for the six months ended October 28, 2017. The Company's effective tax rate decreased to 16.4% for the six months ended October 27, 2018, compared to 17.1% for the six months ended October 28, 2017. The decrease primarily relates to a decrease in pretax income and an increase in investment tax credits during the period.

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Net Income. Net income decreased \$6.4 million, or 14.3%, to \$38.3 million for the six months ended October 27, 2018, compared to \$44.7 million for the six months ended October 28, 2017. Net income decreased due primarily to higher intangible asset amortization, higher stock award amortization, higher acquisition-related costs, customer pricing reductions and higher interest expenses, partially offset by lower legal fees and increased sales volumes and net income from our new acquisitions and higher sales of our radio remote control products.

## Operating Segments

## Automotive Segment Results

Below is a table summarizing results for the six months ended:

| (Dollars in Millions)               | October 27,<br>2018 | October 28,<br>2017 | Net Change<br>(\$) | Net Change<br>(%) |   |
|-------------------------------------|---------------------|---------------------|--------------------|-------------------|---|
| Net Sales                           | \$ 376.9            | \$ 343.2            | \$ 33.7            | 9.8               | % |
| Cost of Products Sold               | 275.0               | 244.5               | 30.5               | 12.5              | % |
| Gross Profit                        | 101.9               | 98.7                | 3.2                | 3.2               | % |
| Selling and Administrative Expenses | 29.1                | 19.5                | 9.6                | 49.2              | % |
| Amortization of Intangibles         | 3.1                 | 0.5                 | 2.6                | 520.0             | % |
| Income from Operations              | \$ 69.7             | \$ 78.7             | \$ (9.0)           | (11.4)            | % |

| Percent of sales:                   | October 27,<br>2018 | October 28,<br>2017 |   |  |
|-------------------------------------|---------------------|---------------------|---|--|
| Net Sales                           | 100.0               | % 100.0             | % |  |
| Cost of Products Sold               | 73.0                | % 71.2              | % |  |
| Gross Margins                       | 27.0                | % 28.8              | % |  |
| Selling and Administrative Expenses | 7.7                 | % 5.7               | % |  |
| Amortization of Intangibles         | 0.8                 | % 0.1               | % |  |
| Income from Operations              | 18.5                | % 22.9              | % |  |

Net Sales. Automotive segment net sales increased \$33.7 million, or 9.8%, to \$376.9 million for the six months ended October 27, 2018, from \$343.2 million for the six months ended October 28, 2017. Net sales increased in North America by \$35.1 million, or 17.9%, to \$231.6 million for the six months ended October 27, 2018, compared to \$196.5 million for the six months ended October 28, 2017. North American Automotive sales included \$6.1 million from Grakon, which was acquired in the second quarter of fiscal 2019, and \$45.1 million from Pacific Insight, which was acquired in the second quarter of fiscal 2018. The second quarter of fiscal 2019 included approximately six weeks of Grakon's results. The first half of fiscal 2018 included only one month of Pacific Insight's results, which included \$6.9 million of net sales. Other North American sales increased for our human machine interface assembly products due to new program launches. Sales declined for our integrated center stack products primarily due to pricing reductions. Sales for our transmission lead-frame assemblies decreased due to a combination of pricing reductions and lower sales volumes. Net sales increased in Europe by \$3.6 million, or 3.6%, to \$102.8 million for the six months ended October 27, 2018, compared to \$99.2 million for the six months ended October 28, 2017. The increase in European sales includes an increase of \$7.9 million from Procoplast, due primarily to only three months of activity being included in the six months ended October 28, 2017. Other European sales decreased primarily due the exclusion of pre-production reimbursements from net sales due to the adoption of ASC 606 on April 29, 2018, partially offset by higher sales volumes of sensor products. European pre-production reimbursements were \$7.1 million during the six months ended October 28, 2018. Net sales in Asia decreased \$5.0 million, or 10.5%, to \$42.5 million for the six months ended October 27, 2018, compared to \$47.5 million for the six months ended October 28, 2017, primarily due to lower sales of our transmission lead-frame assemblies due to a combination of pricing reductions and lower sales volumes. We also experienced lower sales volumes for our steering angle sensor products, as the products approach

end of production. Translation of foreign operations' net sales increased reported net sales by \$1.1 million, or 0.3%, for the six months ended October 27, 2018, compared to the average currency rates for the six months ended October 28, 2017, primarily due to the strengthening of the euro and Chinese yuan as compared to the U.S. dollar.

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**Cost of Products Sold.** Automotive segment cost of products sold increased \$30.5 million, or 12.5%, to \$275.0 million for the six months ended October 27, 2018, from \$244.5 million for the six months ended October 28, 2017. The Automotive segment cost of products sold as a percentage of net sales increased to 73.0% for the six months ended October 27, 2018, compared to 71.2% for the six months ended October 28, 2017. The cost of products sold as a percentage of net sales increased primarily due to sales mix related to our Pacific Insight business, which currently has a higher costs of products sold as a percentage of sales compared to other reporting units within the Automotive segment. In addition, the results of the second half of fiscal 2018, included only one month of Pacific Insight's results. The cost of products sold as a percentage of net sales also increased due to pricing reductions on certain products, partially offset by the weakening of the Mexican peso as compared to the U.S. dollar during the period.

**Gross Profit.** Automotive segment gross profit increased \$3.2 million, or 3.2%, to \$101.9 million for the six months ended October 27, 2018, as compared to \$98.7 million for the six months ended October 28, 2017. The Automotive segment gross margins as a percentage of net sales decreased to 27.0% for the six months ended October 27, 2018, as compared to 28.8% for the six months ended October 28, 2017. Gross margins as a percentage of net sales decreased due primarily to sales mix related to our Pacific Insight business, which currently has a higher costs of products sold as a percentage of sales compared to other reporting units within the Automotive segment. In addition, the results of the first half of fiscal 2018, included only one month of Pacific Insight's results. The cost of products sold as a percentage of net sales also increased due to pricing reductions on certain products, partially offset by the weakening of the Mexican peso as compared to the U.S. dollar during the period.

**Selling and Administrative Expenses.** Selling and administrative expenses increased \$9.6 million, or 49.2%, to \$29.1 million for the six months ended October 27, 2018, compared to \$19.5 million for the six months ended October 28, 2017. Selling and administrative expenses as a percentage of net sales were 7.7% for the six months ended October 27, 2018, compared to 5.7% for the six months ended October 28, 2017. The increase in selling and administrative expenses is partially attributable to the Pacific Insight and Procoplast businesses, which were not owned by Methode during the entirety of the six months ended October 28, 2017. This accounted for \$5.1 million of the increase. Excluding the activity from our Pacific Insight and Procoplast businesses, expenses increased \$4.5 million due primarily to the increase in stock award amortization expense for our long-term incentive program and higher salary and other personnel costs.

**Amortization of Intangibles.** Amortization of intangibles increased \$2.6 million, or 520.0%, to \$3.1 million for the six months ended October 27, 2018, compared to \$0.5 million for the six months ended October 28, 2017. Amortization of intangibles as a percentage of net sales were 0.8% for the six months ended October 27, 2018, compared to 0.1% for the six months ended October 28, 2017.

**Income from Operations.** Automotive segment income from operations decreased \$9.0 million, or 11.4%, to \$69.7 million for the six months ended October 27, 2018, compared to \$78.7 million for the six months ended October 28, 2017. Income from operations for the six months ended October 27, 2018 decreased due primarily to pricing reductions on certain products, an increase in stock award amortization expense for our long-term incentive program and increased intangible asset amortization expense, partially offset by the income from operations from our Pacific Insight, Procoplast and Grakon businesses, and the weakening of the Mexican peso as compared to the U.S. dollar during the period.

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## Industrial Segment Results

Below is a table summarizing results for the six months ended:

| (Dollars in Millions)               | October 27,<br>2018 | October 28,<br>2017 | Net Change<br>(\$) | Net Change<br>(%) |     |
|-------------------------------------|---------------------|---------------------|--------------------|-------------------|-----|
| Net Sales                           | \$ 79.6             | \$ 50.5             | \$ 29.1            | 57.6              | %   |
| Cost of Products Sold               | 55.0                | 37.4                | 17.6               | 47.1              | %   |
| Gross Profit                        | 24.6                | 13.1                | 11.5               | 87.8              | %   |
| Selling and Administrative Expenses | 10.9                | 7.9                 | 3.0                | 38.0              | %   |
| Amortization of intangibles         | 1.5                 | 0.1                 | 1.4                | N/M               | *   |
| Income from Operations              | \$ 12.2             | \$ 5.1              | \$ 7.1             | 139.2             | % * |
| Percent of sales:                   | October 27,<br>2018 | October 28,<br>2017 |                    |                   |     |
| Net Sales                           | 100.0               | % 100.0             | %                  |                   |     |
| Cost of Products Sold               | 69.1                | % 74.1              | %                  |                   |     |
| Gross Margins                       | 30.9                | % 25.9              | %                  |                   |     |
| Selling and Administrative Expenses | 13.7                | % 15.6              | %                  |                   |     |
| Amortization of intangibles         | 1.9                 | % 0.2               | %                  |                   |     |
| Income from Operations              | 15.3                | % 10.1              | %                  |                   |     |

\* N/M equals non-meaningful

**Net Sales.** Industrial segment net sales increased \$29.1 million, or 57.6%, to \$79.6 million for the six months ended October 27, 2018, from \$50.5 million for the six months ended October 28, 2017. Net sales increased in North America by \$20.8 million, or 111.2%, to \$39.5 million for the six months ended October 27, 2018, compared to \$18.7 million for the six months ended October 28, 2017. Net sales in North America includes \$18.1 million from Grakon and represents approximately six weeks of results. Other North American sales increased due primarily to sales volumes of radio remote control and busbar products. Net sales in Europe increased \$2.1 million, or 10.4%, to \$22.2 million for the six months ended October 27, 2018 compared to \$20.1 million for the six months ended October 28, 2017, primarily due to higher sales volumes of radio remote control products, partially offset with lower sales volumes of bypass switches. Net sales in Asia increased \$6.2 million, or 53.0%, to \$17.9 million for the six months ended October 27, 2018, compared to \$11.7 million for the six months ended October 28, 2017, primarily due to higher sales volumes of busbar products.

**Cost of Products Sold.** Industrial segment cost of products sold increased \$17.6 million, or 47.1%, to \$55.0 million for the six months ended October 27, 2018, compared to \$37.4 million for the six months ended October 28, 2017. Industrial segment cost of products sold as a percentage of net sales decreased to 69.1% for the six months ended October 27, 2018, compared to 74.1% for the six months ended October 28, 2017. Cost of products sold as a percentage of net sales decreased due primarily to a favorable sales mix relating to our Grakon business and increased sales volumes of radio remote control and busbar products. In addition, the first half of fiscal 2019 includes \$2.6 million of purchase accounting related adjustments related to the Grakon acquisition.

**Gross Profit.** Industrial segment gross profit increased \$11.5 million, or 87.8%, to \$24.6 million for the six months ended October 27, 2018, compared to \$13.1 million for the six months ended October 28, 2017. Gross margins as a percentage of net sales increased to 30.9% for the six months ended October 27, 2018, from 25.9% for the six months ended October 28, 2017. Gross margins increased due primarily to a favorable sales mix relating to our Grakon business and increased sales volumes of radio remote control and busbar products. In addition, the first half of fiscal 2019 includes \$2.6 million of purchase accounting related adjustments related to the Grakon acquisition.

**Selling and Administrative Expenses.** Selling and administrative expenses increased \$3.0 million, or 38.0%, to \$10.9 million for the six months ended October 27, 2018, compared to \$7.9 million for the six months ended October 28, 2017. Selling and administrative expenses as a percentage of net sales decreased to 13.7% for the six months ended October 27, 2018,



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from 15.6% for the six months ended October 28, 2017. The results for the six months ended October 27, 2018 include \$5.7 million of selling and administrative expenses from Grakon. Excluding the impacts of the Grakon acquisition, selling and administrative expenses decreased \$2.7 million due primarily to lower legal fees, partially offset by higher stock award amortization expense for our long-term incentive program.

**Amortization of Intangibles.** Amortization of intangibles increased \$1.4 million to \$1.5 million for the six months ended October 27, 2018, compared to \$0.1 million for the six months ended October 28, 2017. Amortization of intangibles as a percentage of net sales increased to 1.9% for the six months ended October 27, 2018, from 0.2% for the six months ended October 28, 2017.

**Income from Operations.** Industrial segment income from operations was \$12.2 million for the six months ended October 27, 2018, compared to \$5.1 million for the six months ended October 28, 2017. Income from operations increased due primarily to lower legal fees, higher sales of radio remote control and busbar products and the income from operations from our Grakon business.

**Interface Segment Results**

Below is a table summarizing results for the six months ended:

| (Dollars in Millions)               | October 27,<br>2018 | October 28,<br>2017 | Net Change<br>(\$) | Net Change<br>(%) |
|-------------------------------------|---------------------|---------------------|--------------------|-------------------|
| Net Sales                           | \$ 30.3             | \$ 37.5             | \$ (7.2 )          | (19.2 )%          |
| Cost of Products Sold               | 25.9                | 29.8                | (3.9 )             | (13.1 )%          |
| Gross Profit                        | 4.4                 | 7.7                 | (3.3 )             | (42.9 )%          |
| Selling and Administrative Expenses | 3.2                 | 3.2                 | —                  | — %               |
| Amortization of Intangibles         | 1.0                 | 1.1                 | (0.1 )             | (9.1 )%           |
| Income from Operations              | \$ 0.2              | \$ 3.4              | \$ (3.2 )          | (94.1 )%          |

| Percent of sales:                   | October 27,<br>2018 | October 28,<br>2017 |
|-------------------------------------|---------------------|---------------------|
| Net Sales                           | 100.0 %             | 100.0 %             |
| Cost of Products Sold               | 85.5 %              | 79.5 %              |
| Gross Margins                       | 14.5 %              | 20.5 %              |
| Selling and Administrative Expenses | 10.6 %              | 8.5 %               |
| Amortization of Intangibles         | 3.3 %               | 2.9 %               |
| Income from Operations              | 0.7 %               | 9.1 %               |

**Net Sales.** Interface segment net sales decreased \$7.2 million, or 19.2%, to \$30.3 million for the six months ended October 27, 2018, compared to \$37.5 million for the six months ended October 28, 2017. Net sales decreased in North America by \$7.0 million, or 19.2%, to \$29.4 million for the six months ended October 27, 2018, compared to \$36.4 million for six months ended October 28, 2017, primarily due to lower sales volumes of appliance and data solution products. Net sales in Asia decreased \$0.3 million, or 27.3%, to \$0.8 million for the six months ended October 27, 2018, compared to \$1.1 million for the six months ended October 28, 2017, due to lower sales volumes of legacy products.

**Cost of Products Sold.** Interface segment cost of products sold decreased \$3.9 million, or 13.1%, to \$25.9 million for the six months ended October 27, 2018, compared to \$29.8 million for the six months ended October 28, 2017. The Interface segment cost of products sold as a percentage of net sales increased to 85.5% for the six months ended October 27, 2018, from 79.5% for the six months ended October 28, 2017. The increase primarily relates to lower sales volumes of our appliance products and lower sales volumes and unfavorable sales mix of our data solutions products, partially offset by the weakening of the Mexican peso as compared to the U.S. dollar during the period.

Gross Profit. Interface segment gross profit decreased \$3.3 million, or 42.9%, to \$4.4 million for the six months ended October 27, 2018, compared to \$7.7 million for the six months ended October 28, 2017. Gross margins as a percentage

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of net sales decreased to 14.5% for the six months ended October 27, 2018 from 20.5% for the six months ended October 28, 2017. The decrease primarily relates to lower sales volumes of our appliance products and lower sales volumes and unfavorable sales mix of our data solutions products, partially offset by the weakening of the Mexican peso as compared to the U.S. dollar during the period.

**Selling and Administrative Expenses.** Selling and administrative expenses were unchanged at \$3.2 million for both the six months ended October 27, 2018 and October 28, 2017, respectively. Selling and administrative expenses as a percentage of net sales increased to 10.6% for the six months ended October 27, 2018 from 8.5% for the six months ended October 28, 2017. During the period, higher stock award amortization expense was offset by lower legal expense.

**Amortization of Intangibles.** Amortization of intangibles decreased \$0.1 million, or 9.1%, to \$1.0 million for the six months ended October 27, 2018, compared to \$1.1 million for the six months ended October 28, 2017. Amortization of intangibles as a percentage of net sales increased to 3.3% for the six months ended October 27, 2018 from 2.9% for the six months ended October 28, 2017.

**Income From Operations.** Interface segment income from operations decreased \$3.2 million, or 94.1%, to \$0.2 million for the six months ended October 27, 2018, compared to \$3.4 million for the six months ended October 28, 2017. Income from operations decreased due primarily to lower sales volumes and unfavorable sales mix, partially offset by the weakening of the Mexican peso as compared to the U.S. dollar during the period.

**Medical Segment Results**

Below is a table summarizing results for the six months ended:

| (Dollars in Millions)               | October 27,<br>2018 | October 28,<br>2017 | Net Change<br>(\$) | Net Change<br>(%) |
|-------------------------------------|---------------------|---------------------|--------------------|-------------------|
| Net Sales                           | \$ 0.6              | \$ 0.1              | \$ 0.5             | 500.0 %           |
| Cost of Products Sold               | 2.0                 | 1.6                 | 0.4                | 25.0 %            |
| Gross Profit                        | (1.4 )              | (1.5 )              | 0.1                | (6.7 )%           |
| Selling and Administrative Expenses | 3.2                 | 4.3                 | (1.1 )             | (25.6 )%          |
| Loss from Operations                | \$ (4.6 )           | \$ (5.8 )           | \$ 1.2             | (20.7 )%          |

**Net Sales.** The Medical segment had \$0.6 million of net sales in the six months ended October 27, 2018 and \$0.1 million of net sales in the six months ended October 28, 2017, due primarily to an expansion in our customer base.

**Cost of Products Sold.** Medical segment cost of products sold was \$2.0 million for the six months ended October 27, 2018, compared to \$1.6 million for the six months ended October 28, 2017. The increase primarily relates to an increase in sales volumes during the period.

**Gross Profit.** The Medical segment gross profit was a loss of \$1.4 million and \$1.5 million for the six months ended October 27, 2018 and October 28, 2017, respectively. The decreased loss primarily relates to an increase in sales volumes during the period.

**Selling and Administrative Expenses.** Selling and administrative expenses decreased \$1.1 million, or (25.6)%, to \$3.2 million for the six months ended October 27, 2018, compared to \$4.3 million for the six months ended October 28, 2017. The decrease in selling and administrative expenses for the six months ended October 27, 2018 primarily relates to decreased marketing expense in the period and lower stock award amortization expense for our long-term incentive program.

**Loss From Operations** The Medical segment loss from operations decreased \$1.2 million to \$4.6 million for the six months ended October 27, 2018, compared to \$5.8 million for the six months ended October 28, 2017. The decreased loss relates to lower selling and administrative expenses related to decreased marketing expense and lower stock award amortization expense in the period.



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## Liquidity and Capital Resources

We believe our current world-wide cash balances together with expected future cash flows to be generated from operations and our committed credit facility will be sufficient to support current operations. A significant amount of cash and expected future cash flows are located outside of the U.S. Of the \$110.9 million of cash and cash equivalents as of October 27, 2018, \$96.7 million was held in subsidiaries outside the U.S. and \$72.7 million of this amount is deemed to be permanently reinvested.

On September 12, 2018, the Company entered into an Amended and Restated Credit Agreement with Bank of America, N.A., as Administrative Agent, Swing Line Lender and L/C Issuer, Wells Fargo Bank, National Association, as L/C Issuer, and the Lenders named therein (the "Credit Agreement"). The Credit Agreement amends and restates the Credit Agreement, dated November 18, 2016 (the "Existing Credit Agreement"), among the Company, Bank of America, N.A., as Administrative Agent, Swing Line Lender, and L/C Issuer, Wells Fargo Bank, National Association, as L/C Issuer, and the Lenders named therein. The Credit Agreement has a maturity date of September 12, 2023. The Credit Agreement includes a senior unsecured revolving credit facility, as well as a senior unsecured term loan, and is guaranteed by the Company's wholly-owned U.S. subsidiaries.

The revolving credit facility has a maximum principal amount of \$200.0 million and is available for general corporate purposes, including working capital and acquisitions. The term loan has a principal amount of \$250.0 million and was made to partially fund the acquisition of Grakon in the second quarter of fiscal 2019. The Credit Agreement contains an option to increase the aggregate principal amount of the revolving credit facility and term loan by up to an additional \$200.0 million, subject to customary conditions and approval of the lender(s) providing new commitment(s). The Credit Agreement provides for variable rates of interest based on the type of borrowing and the Company's debt to EBITDA financial ratio and contains customary representations and warranties, financial covenants, restrictive covenants and events of default. At October 27, 2018, the interest rate on both the revolving credit facility and term loan was 1.50% plus LIBOR and we were in compliance with the covenants of the agreement. During the six months ended October 27, 2018, we had \$98.0 million of borrowings, including the \$250.0 million term loan, and payments of \$41.5 million, which includes interest of \$1.5 million, under the Credit Agreement. As of October 27, 2018, there were outstanding balances of \$88.0 million and \$250.0 million against the revolving credit facility and term loan, respectively. We believe the fair values approximate the carrying amounts as of October 27, 2018.

Methode's subsidiary, Pacific Insight, is party to a credit agreement with the Bank of Montreal. The credit agreement with the Bank of Montreal has a maturity date of December 21, 2019 and provides a credit facility in the maximum principal amount of C\$10.0 million, with an option to increase the principal amount by up to an additional C\$5.0 million. Availability under the facility is determined based upon a percentage of eligible accounts receivable and finished goods inventory balances and funds are available in either Canadian or U.S. currency. Interest is calculated at either the Canadian Dollar Offered Rate plus 1.25%, the Federal Funds Rate plus 1.25% or LIBOR plus 1.75%. As of October 27, 2018, there were no outstanding balances against this credit facility and Pacific Insight was in compliance with the covenants of the agreement.

In addition to the credit agreement with the Bank of Montreal, Pacific Insight was, until the second quarter of fiscal 2019, party to a credit agreement with Roynat. The credit agreement between Pacific Insight and Roynat was terminated during the second quarter of fiscal 2019 and payments of \$2.8 million were made upon termination, including a prepayment fee of \$0.1 million. Total repayments under this credit facility in fiscal 2019 were \$3.8 million.

Excluding credit facilities, the Company also holds debt at its Procoplast subsidiary. As of October 27, 2018, Procoplast holds short-term debt totaling \$3.0 million, with a weighted average interest rate of 1.75%. As of October 27, 2018, Procoplast holds long-term debt that consists of seventeen notes totaling \$16.8 million, with a weighted-average interest rate of 1.48% and maturities ranging from 2019 to 2031.

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## Cash Flow - Operating Activities

Net cash provided by operating activities decreased \$9.0 million to \$36.2 million for the six months ended October 27, 2018, compared to \$45.2 million for the six months ended October 28, 2017, primarily due to the changes in operating assets and liabilities, partially offset by an increase in our net income, adjusted for depreciation, amortization, deferred tax expense, stock-based compensation and the provision for bad debt. For the six months ended October 27, 2018, net changes in operating assets and liabilities resulted in cash used of \$41.4 million, primarily due to an increase in prepaid expenses and other assets, an increase in accounts receivable, a decrease in accounts payable and other expenses and an increase in inventory levels. For the six months ended October 28, 2017, net changes in operating assets and liabilities resulted in cash used of \$19.7 million, primarily due to an increase in accounts receivable, an increase in prepaid expenses and other assets and an increase in inventory levels, partially offset by a decrease in accounts payable and other expenses.

## Cash Flow - Investing Activities

Net cash used in investing activities was \$449.5 million for the six months ended October 27, 2018, compared to \$146.0 million for the six months ended October 28, 2017. Net cash used in investing activities for the six months ended October 27, 2018 included \$421.6 million, net of cash acquired, for the acquisition of Grakon. Net cash used in investing activities for the six months ended October 28, 2017 included \$129.9 million, net of cash acquired, for the acquisitions of Pacific Insight and Procoplast. Net cash used for the purchase of property, plant and equipment was \$28.6 million for the six months ended October 27, 2018, compared to \$16.4 million for the six months ended October 28, 2017.

## Cash Flow - Financing Activities

Net cash provided by financing activities increased \$239.9 million to \$291.1 million for the six months ended October 27, 2018, compared to \$51.2 million for the six months ended October 28, 2017. During the six months ended October 27, 2018, the Company had \$348.0 million of borrowings against credit facilities, as compared to \$129.9 million during the six months ended October 28, 2017. During the six months ended October 27, 2018, the Company had repayments of borrowings against credit facilities and other debt of \$46.6 million, compared to \$2.8 million during the six months ended October 28, 2017. We paid dividends of \$8.6 million and \$6.8 million in the six months ended October 27, 2018 and October 28, 2017, respectively. The first six months of fiscal 2019 included \$1.7 million of taxes paid related to net share settlement of equity awards, compared to \$0.3 million during the first six months of fiscal 2018. There were no proceeds from the exercise of stock options in either the first six months of fiscal 2019 or the first six months of fiscal 2018.

## Off-Balance Sheet Arrangements

We do not have any off-balance sheet arrangements, other than operating leases and purchase obligations entered into in the normal course of business.

## Item 3. Quantitative And Qualitative Disclosures About Market Risk

Certain of our foreign operations enter into transactions in currencies other than their functional currency, primarily the U.S. dollar and the euro. A 10% change in foreign currency exchange rates from balance sheet date levels could impact our income before income taxes by \$2.2 million as of October 27, 2018 and \$1.9 million as of April 28, 2018. We also have foreign currency exposure arising from the translation of our net equity investment in our foreign operations to U.S. dollars. We generally view our investments in foreign operations with functional currencies other than the U.S. dollar as long-term. The currencies to which we are exposed are the British pound, Canadian dollar, Chinese yuan, euro, Indian rupee, Mexican peso, Singapore dollar and Swiss franc. A 10% change in foreign currency exchange rates from balance sheet date levels could impact our net foreign investments by \$40.0 million at October 27, 2018 and \$49.3 million at April 28, 2018.

We are exposed to market risk from changes in interest rates. The interest rate risk for our credit agreements, under which we had \$338.0 million of net borrowings at October 27, 2018, is variable and is determined based on LIBOR. We estimate that a one percentage point change in interest rates would not have a material impact on our results of operations for fiscal 2019 based upon our current and expected levels of debt.

Item 4. Controls And Procedures

As of the end of the period covered by this quarterly report on Form 10-Q, we performed an evaluation under the supervision and with the participation of the Company's management, including our Chief Executive Officer and our Chief Financial Officer, of our "disclosure controls and procedures" (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities

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Exchange Act of 1934). The Company's disclosure controls and procedures are designed to ensure that the information required to be disclosed by the Company in the reports that we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's applicable rules and forms. As a result of this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were effective.

There have been no changes in our internal control over financial reporting during the quarter ended October 27, 2018 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.



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## PART II. OTHER INFORMATION

## Item 1A. Risk Factors

Other than the supplemental risk factors set forth below, there have been no material changes to the risk factors disclosed in Part I - Item 1A, Risk Factors of our Form 10-K for the fiscal year ended April 28, 2018.

International trade disputes could result in tariffs and other protectionist measures that could adversely affect the Company's business.

Tariffs could increase the cost of the Company's products and the components and raw materials that go into making them. These increased costs could adversely impact the gross margin that the Company earns on sales of its products. Tariffs could also make the Company's products more expensive for customers, which could make the Company's products less competitive and reduce consumer demand. Countries may also adopt other protectionist measures that could limit the Company's ability to offer its products and services. Political uncertainty surrounding international trade disputes and protectionist measures could also have a negative effect on consumer confidence and spending, which could adversely affect the Company's business.

Any changes in U.S. trade policy could trigger retaliatory actions by affected countries, resulting in 'trade wars.' Any changes in U.S. trade policy could trigger retaliatory actions by affected countries, resulting in 'trade wars,' which could increase costs for goods imported into the United States. This increase in costs may reduce customer demand for these products if the parties having to pay those tariffs increase their prices, or if trading partners limit their trade with the United States. If these consequences are realized, the volume of economic activity in the United States, including demand for our products, may be materially reduced. Such a reduction may materially and adversely affect our sales and our business.

## Item 6. Exhibits

| Exhibit<br>Number | Description |
|-------------------|-------------|
|-------------------|-------------|

|       |  |
|-------|--|
| 10.1  | <u>Agreement and Plan of Merger dated August 20, 2018 by and among Methode Electronics, Inc., Flash Merger Sub Corp., Grakon Parent, Inc., and Industrial Growth Partners IV, L.P.</u> |
| 31.1  | <u>Rule 13a-14(a)/15d-14(a) Certification of Principal Executive Officer</u>   |
| 31.2  | <u>Rule 13a-14(a)/15d-14(a) Certification of Principal Financial Officer</u>   |
| 32    | <u>Certification of Periodic Financial Report Pursuant to 18 U.S.C. Section 1350</u>   |
| 101.1 | XBRL Instance  |
| 101.2 | XBRL Taxonomy Extension Schema Document  |
| 101.3 | XBRL Taxonomy Extension Calculation Linkbase Document  |
| 101.4 | XBRL Taxonomy Extension Label Linkbase Document  |
| 101.5 | XBRL Taxonomy Extension Presentation Linkbase Document   |
| 101.6 | XBRL Taxonomy Extension Definition Linkbase Document   |

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SIGNATURES

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

METHODE  
ELECTRONICS, INC.

By: /s/ Ronald L.G. Tsoumas  
Ronald L.G. Tsoumas  
Chief Financial Officer  
(principal financial officer)

Dated: December 6, 2018