

PULSE ELECTRONICS CORP
Form 10-K
March 13, 2013

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

FORM 10-K

Annual Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the fiscal year ended December 28, 2012

or

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

Commission File No. 1-5375

PULSE ELECTRONICS CORPORATION
(Exact name of registrant as specified in Charter)

PENNSYLVANIA
(State or other jurisdiction of Incorporation or
organization)

23-1292472
(IRS Employer Identification Number)

12220 World Trade Drive, San Diego, California
(Address of principal executive offices)
Registrant's telephone number, including area code:

92128
(Zip Code)
858-674-8100

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

Title of each class
Common Stock par value \$0.125 per share

Name of each Exchange on which registered
New York Stock Exchange

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such

files). Yes No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer (as defined in Rule 12b-2 of the Act). Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

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

The aggregate market value of voting stock held by non-affiliates as of June 30, 2012 is \$81,770,000 computed by reference to the closing price on the New York Stock Exchange on such date.

Title of each class	Number of shares outstanding March 13, 2013
Common stock par value \$0.125 per share	79,473,375

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive proxy statement to be used in connection with the registrant's 2013 Annual Shareholders Meeting are incorporated by reference into Part III of this Form 10-K where indicated.

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Cautionary Note Regarding Forward-Looking Statements

Our disclosures and analysis in this report contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21A of the Securities Exchange Act of 1934. Forward-looking statements reflect our current expectations of future events or future financial performance. You can identify these statements by the fact that they do not relate strictly to historical or current facts. They often use words such as “anticipate”, “estimate”, “expect”, “project”, “intend”, “plan”, “believe” and other similar terms. These forward-looking statements are based on our current plans and expectations. We intend that all forward-looking statements be subject to the “safe harbor” provisions of the Private Securities Litigation Reform Act of 1995.

Any or all of our forward-looking statements in this report may prove to be incorrect. They may be affected by inaccurate assumptions we might make or by risks and uncertainties which are either unknown or not fully known or understood. Accordingly, actual outcomes and results may differ materially from what is expressed or forecasted in this report.

We sometimes provide forecasts of future financial performance and liquidity. The risks and uncertainties described under “Risk Factors” as well as other risks identified from time to time in other Securities and Exchange Commission reports, registration statements and public announcements, among others, should be considered in evaluating our prospects for the future. We undertake no obligation to release updates or revisions to any forward-looking statement, whether as a result of new information, future events or otherwise.

Part I

Item 1 Business

General

We were incorporated in Pennsylvania on April 10, 1947 and are headquartered in San Diego, California. Our mailing address is 12220 World Trade Drive, San Diego, CA 92128-3797, and our telephone number is 858-674-8100. Our website is www.pulseelectronics.com. Information contained on our website shall not be deemed to be incorporated into this Annual Report. Our ticker symbol on the New York Stock Exchange is “PULS.”

Pulse Electronics Corporation is a global producer of precision-engineered electronic components and modules. We sometimes refer to Pulse Electronics Corporation as “Pulse Electronics”, “Pulse”, “the Company”, “we” or “our.” Based on our estimates of the total annual revenues in our primary markets and our share of those markets relative to our competitors, we believe we are a leading global producer of electronic components and modules in the primary markets we serve.

We operate our business in three segments: our Network product group (“Network”), our Power product group (“Power”) and our Wireless product group (“Wireless”).

Network

Network produces a variety of passive components that manage and regulate electronic signals for use in a variety of devices used in local area and wide area networks. These products operate by filtering out radio frequency interference, shaping waveforms, splitting signals, suppressing noise, matching impedances and other functions. These passive products are often referred to as connectors, filters, filtered connectors, transformers, splitters, micro-filters, baluns and chokes.

Network's components are characterized by labor intensive manufacturing processes that can be highly customized. Generally, our Network products have relatively short life cycles due to process and cost improvements, which allow us to utilize our design, engineering and production expertise to meet our customers' evolving needs. The markets Network serves have been, and are expected to be, characterized by ongoing product design and manufacturing innovation.

Network generated \$158.1 million, or 42.4% of our revenues, for the year ended December 28, 2012 and \$169.8 million, or 46.0% of our revenues, for the year ended December 30, 2011. Refer to Note 19, Segment and geographical information, to the Consolidated Financial Statements for additional information regarding our segments.

Power

Power primarily manufactures products that adjust and ensure proper current and voltage, limit distortion of voltage, sense and report current and voltage and cause mechanical movement or actuation. Power's products include power transformers, chokes, current and voltage sensors, ignition coils, automotive coils, military and aerospace products and other power magnetic products.

While some of Power's manufacturing is characterized by labor intensive processes, other portions of the business are highly automated and less variable with product life cycles that change as technology improves. These factors allow us to utilize our design, engineering and production expertise to meet our customer design needs. The markets Power serves have been, and will continue to be, characterized by ongoing product design and manufacturing innovation.

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Power generated \$120.2 million, or 32.2 % of our revenues, for the year ended December 28, 2012 and \$135.2 million, or 36.6% of our revenues, for the year ended December 30, 2011. Refer to Note 19, Segment and geographical information, to the Consolidated Financial Statements for additional information regarding our segments.

Wireless

Wireless manufactures products that primarily capture or transmit wireless communication signals. Specifically, our Wireless segment produces antennas, antenna modules and antenna mounting components that capture and transmit communication signals in handsets, other terminal and portable devices, automobiles and wireless-to-wireline access points.

Our Wireless products are sold in a very dynamic market, which causes the life of an average Wireless product to be very short. Wireless utilizes our expertise in the design, engineering and production of antennas and antenna modules to evolve with our customer needs. We believe that the industries Wireless serves have been, and will continue to be, characterized by ongoing product design and manufacturing innovation. However, the manufacturing of our Wireless products tends to be more automated than Network and many Power products, requiring capital investment and changes in our production process for future innovation.

Wireless generated \$94.9 million, or 25.4% of our revenues, for the year ended December 28, 2012 and \$64.3 million, or 17.4% of our revenues, for the year ended December 30, 2011. Refer to Note 19, Segment and geographical information, to the Consolidated Financial Statements for additional information regarding our segments.

Products

The following table contains a list of some of the key products of our segments:

Primary Products	Function	Application
Network		
Discrete filter or choke	Separate high and low frequency signals, share incoming and outgoing signals to match industry templates	Network switches, routers, hubs and personal computers Phone, fax and alarm systems used with digital subscriber lines or DSL
Filtered connectors, which combines a filter with a connector and stand alone connector products	Remove interference, or noise, from circuitry and connects electronic equipment	Local area networks, or LANs, and wide area networks, or WANs, equipment for personal computers and video game consoles
Inductor/chip inductor	Regulate and control electrical energy in a communication circuit	AC/DC & DC/DC power supplies Mobile phones and portable devices
Balun	Connect lines that are balanced to lines that are unbalanced	Cable television and other networks carrying high frequency signals

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Transformer	Transfer electrical energy from one circuit to another and provide an impedance match between circuits	Electronic devices that are connected by a wire including PCs, laptops, game boxes, network switches, telephone equipment and DSL routers.
Splitter and diplexer	Split communication signals for further processing	Wide Area and telephone networks and cable television systems
Power		
Power transformer	Modify circuit voltage	AC/DC & DC/DC power supplies or, generally, anything that plugs in for power
Signal transformer	Limit distortion of signals as they pass from one medium to another	Analog circuitry, military/aerospace navigation and weapons guidance systems
Automotive ignition coils	Provide power for automotive ignition	Ignition systems for automotive gasoline engines
Other automotive coils	Provide power for a variety of automotive electronic functions. Create or control mechanical movement.	Automotive management systems such as safety, communication, navigation, fuel efficiency and emissions control
Inductor/chip inductor	Regulate and control electrical energy under conditions of varying loads	Point of load conversion for power on various electronic devices, including servers, switches, computers, game boxes and telephone network equipment
Current and voltage sensors	Sense the presence of, amount of or phase of current or voltage	Inverters, smart meters, charging stations, electric grid control, flight power generation, motor control and industrial control
Wireless		
Internal handset antenna and handset antenna modules	Capture and transmit communication signals in mobile handsets, personal digital assistants and notebook computers	Cell phones, other terminal and information devices
Mobile and portable antennas	Capture and transmit non-cellular wireless signals, including blue tooth, GPS, WiFi, RFID, VHF/UHF and DECT	Global positioning systems, automotive antennas, wireless handsets, femtocells, routers, switches, smart meters, mesh networks and machine-to-machine communication
Mounts and cables	Mount an antenna onto mobile or	Police cars, fire trucks, delivery

stationary location

vehicles, lamp posts, rail cars and
other automobiles

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Sales, Customers and Distribution

Each of our segments sell products predominantly through our worldwide direct sales forces. Given the highly technical nature of our customers' needs, our direct salespeople typically team up with members of our engineering staff to discuss a sale with a customer's purchasing and engineering personnel. During the sales process, there is close interaction between our engineers and those in our customers' organizations. This interaction extends throughout a product's life cycle, engendering strong customer relationships. Also, we believe that our coordinated sales effort provides a high level of market penetration and efficient coverage of our customers on a cost-effective basis. As of December 28, 2012, we had approximately 53 salespeople in 8 sales offices worldwide.

We sell our products and services to original equipment manufacturers, original design manufacturers and electronic contract equipment manufacturers, which design, build and market end-user products. We refer to these companies as OEMs, ODMs and CEMs, respectively. ODMs typically contract with OEMs to design products, whereas CEMs contract with OEMs to manufacture products. Many OEMs use CEMs primarily or exclusively to build their products. Independent distributors sell components and materials to both OEMs and CEMs. While OEMs are often our design partners, most sales are to CEMs, as OEMs have generally outsourced procurement and manufacturing responsibilities to CEMs. In order to maximize our sales opportunities, our engineering and sales teams maintain close relationships with all outlets, including OEMs, ODMs, CEMs and other independent distributors. We provide support for our multinational customer base with local customer service and design centers in North America, Europe and Asia.

For the year ended December 28, 2012, no single customer accounted for more than 10% of our consolidated net sales. However, one customer in our Network segment, when aggregated with their CEM suppliers, represents more than 10% of our business. Sales to our 10 largest customers accounted for 50.1% of net sales for the year ended December 28, 2012, 47.5% of net sales for the year ended December 30, 2011 and 54.1% of net sales for the year ended December 31, 2010.

A large percentage of our net sales are made outside of the United States. For the years ended December 28, 2012, December 30, 2011 and December 31, 2010, 87.6%, 86.4%, and 84.2% of our net sales were outside of the United States, respectively.

Manufacturing

We have developed custom manufacturing processes intended to maximize production efficiency without sacrificing the quality of our products. Specifically, Network's manufacturing of magnetic components, connectors, chokes and filters is labor intensive and can be highly variable. Our model enables flexibility of production to contain costs during slower periods, which reflects the often unpredictable nature of market demand for our product lines. As the cost of labor increases, we are making investments in automation for this product line. However, our model may also prevent us from increasing production capacity over periods of intense demand in tight labor markets. Conversely, the manufacturing of our antennas, automotive and military/aerospace products of our Wireless and Power segments is highly mechanized or, in some cases, automated, which causes costs and profitability related to these products to be sensitive to the volume of production.

Generally, once our engineers design products to meet the end users' needs and a contract is awarded by, or orders are received from, the customer we begin to mass produce the products. To a much lesser extent, we also service customers that design their own components and outsource production of these components to us. In such case, we build the components to the customer's design. We also maintain a portfolio of catalog parts which our customers can easily design into their own products.

We cannot accurately estimate or forecast the overall utilization of our production capacity at a given time. In each facility, maximum capacity and utilization periodically vary depending on our manufacturing strategies, the product being manufactured, current market conditions, customer demand and other non-specific variables.

Research, Development and Engineering

Our research, development and engineering efforts are focused on the design and development of innovative products in collaboration with our customers or their ODM partners. We work closely with OEMs and ODMs to identify their design and engineering requirements. We have design centers throughout the world in proximity to customers to enable better understanding of our end products and readily satisfy our customers' design and engineering needs. Our product lifecycle management system tracks the level of design activity per customer. This enables us to manage and improve our engineers' processes for designing products, which has created an overall disciplined and orderly design methodology. We typically own the customized designs used to make our products.

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Research, development and engineering expenditures were \$24.9 million for the year ended December 28, 2012, \$26.7 million for the year ended December 30, 2011 and \$29.7 million for the year ended December 31, 2010. In limited circumstances, we generate revenue as a result of providing research, development and engineering services to our customers. However, this revenue is not material to our Consolidated Financial Statements.

Competition

We do not believe that any one company competes with the breadth of our product lines on a global basis. However, each of our segments has strong competition within individual product lines, both domestically and internationally. In addition, several OEMs internally, or through CEMs, manufacture certain of our product offerings. We pursue opportunities to demonstrate to OEMs that our economies of scale, purchasing power and core competencies in manufacturing enable us to produce these products more efficiently. Increasingly, we compete against manufacturers located in low cost of labor countries, many of which sometimes aggressively seek market share at the detriment of profits.

Competitive factors in the markets for our products include:

engineering expertise;
product quality and reliability;
global design and manufacturing capabilities;
breadth of product line;
price;
customer service; and
delivery time.

We believe we are competitive with respect to each of these factors. Product quality and reliability, as well as design and manufacturing capabilities, are enhanced through our continuing commitment to invest in and improve our manufacturing and design resources and, also, our close relationships with our customers' engineers. In addition, the breadth of our segments' product offerings provides customers with the ability to satisfy multiple needs through one supplier. Also, our global presence enables us to deepen our relationships with customers and to better understand and more easily satisfy their needs in local markets. Our ability to purchase raw materials in large quantities reduces our production expenses, maximizes our capacity, continually lowers our manufacturing costs and enables us to price our products competitively.

Employees

As of December 28, 2012, we had approximately 12,000 full-time employees compared to 14,000 at December 30, 2011. We utilize temporary staff to supplement our labor capacity, and we have excluded temporary staff from our full-time employment figures. Approximately 230 full-time employees were located in the United States. None of our employees were covered by collective-bargaining agreements during the year ended December 28, 2012. Also, we did not experience any major work stoppages during 2012, and we consider relationships with our employees to be in good standing.

Raw Materials

The primary raw materials necessary to manufacture all our segments' products include:

base metals such as copper;
ferrite cores;

plastics and plastic resins; and
rare earth metals.

Currently, we do not have significant difficulty obtaining any raw materials integral to our manufacturing and do not anticipate that we will face any significant difficulty in the near future. However, some of these materials are produced by a limited number of suppliers. The limited amount of suppliers may restrict our ability to obtain these raw materials in sufficient quantities, at reasonable prices or in a timely manner to meet our customers' demand for our products. A lack of availability or a delay in obtaining any of the raw materials used in our products could adversely affect our manufacturing costs and profit margins. In addition, if the price of our raw materials increases significantly over a short period of time due to increased market demand or shortage of supply, customers may be unwilling to bear the increased price for our products and we may be forced to sell our products containing these materials at lower prices causing a reduction in our profit margins.

Backlog

Our backlog of unfilled orders at December 28, 2012 and December 30, 2011 was approximately \$36.1 million and \$40.7 million, respectively. Orders typically fluctuate from quarter to quarter based on customer demand and general business conditions. Unfilled orders may be canceled prior to shipment of goods. It is expected that all or a substantial portion of the backlog will typically be filled within six months. We do not believe that our backlog is an accurate indicator of near-term business activity because of variability in lead times, capacity, and demand uncertainty on the part of our customers, and, also, the increased use of vendor managed inventory and similar consignment type arrangements, tend to limit the significance of our backlog.

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Intellectual Property

We utilize proprietary technology that is often developed and protected by us or, to a much lesser extent, licensed from others. Also, we require each of our employees with access to proprietary technology to enter into confidentiality agreements. We also restrict access to our proprietary information to only those employees essential to our products' creation.

Existing legal protections afford only limited advantage to us. For example, others may independently develop similar or competing products or attempt to copy or use aspects of our products that we regard as proprietary. Furthermore, intellectual property law in certain areas of the world may not fully protect our products or technology from such actions. While our intellectual property is important to us in the aggregate, we do not believe any individual patent, trademark or license is material to our business or operations.

Environmental

Our manufacturing operations are subject to a variety of local, state, federal and international environmental laws and regulations governing air emissions, wastewater discharges, the storage, use, handling, disposal and remediation of hazardous substances and, also, employee health and safety. It is our policy to meet or exceed the environmental standards set by these laws. Through planning and continual process improvements, we strive to protect and preserve the environment by preventing pollution and reducing the consumption of natural resources and materials. However, in the normal course of business, environmental issues may arise. We may incur increased costs associated with environmental compliance and cleanup projects necessitated by the identification of new environmental issues or new environmental laws and regulations.

Available Information

We make available free of charge on our website, www.pulseelectronics.com, all materials that we file electronically with the Securities and Exchange Commission ("SEC"), including our annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports and all Board and Committee charters, as soon as reasonably practicable after we electronically file or furnish such materials to the SEC.

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Item 1a

Risk Factors

You should carefully consider the following risks and any of the other information set forth in this Annual Report on Form 10-K and in the documents incorporated herein by reference, before deciding to invest in shares of our common stock. The risks described below are not the only ones that we face. Additional risks that are not presently known to us or that we currently deem immaterial may also impair our business operations. The following risks, among others, could cause our actual results, performance, achievements or industry results to differ materially from those expressed in our forward-looking statements contained herein and presented elsewhere by management from time to time. If any of the following risks actually occurs, our business prospects, financial condition or results of operations could be materially harmed and the market price of our common stock would likely decline due to the occurrence of any of these risks.

Cyclical changes in the markets we serve could result in a significant decrease in demand for our products, which may reduce our profitability and/or our cash flow.

Our components are used in various products sold in the electronics market. Generally, these markets are cyclical based on the end consumers' demand, so interest in our components also reflects the overall demand for products in the electronics market. A contraction in the electronics market would result in a decrease in sales of our products, as our customers:

- may cancel existing orders;
- may introduce fewer new products;
- may discontinue current product lines; and
- may decrease their inventory levels.

A decrease in demand for our products could have a significant adverse effect on our operating results, profitability and cash flows, which may adversely affect our liquidity, our ability to retire debt or our ability to comply with debt covenants. Accordingly, we may experience volatility in our revenues, profits and cash flows.

Our debt levels could adversely affect our financial position, our liquidity and the perception of our financial condition in the financial markets.

We have a significant amount of indebtedness. As of December 28, 2012, we had aggregate long-term indebtedness, excluding debt discounts, of approximately \$125.8 million.

Subject to the limits contained in the credit agreement governing our senior credit facility and our outstanding 7.0% senior convertible notes due December 15, 2014 (the "senior convertible notes"), we may choose to incur substantial additional debt from time to time to finance working capital, capital expenditures, investments or acquisitions, or for other purposes. If we do so, the risks related to our high level of debt could intensify. Specifically, our high level of debt could have important consequences, including:

- limiting our ability to obtain additional financing to fund future working capital, capital expenditures, acquisitions or other general corporate requirements;
- requiring a substantial portion of our cash flow to be dedicated to debt service payments instead of other purposes, thereby reducing the amount of cash flow available for working capital, capital expenditures, acquisitions and other general corporate purposes;
- increasing our vulnerability to adverse changes in general economic, industry and competitive conditions;
- limiting our flexibility in planning for and reacting to changes in the industry in which we compete;

placing us at a disadvantage compared to other, less leveraged competitors or competitors with comparable debt at more favorable interest rates; and

increasing our costs of borrowing.

The terms of our debt restrict our current and future operations, particularly our ability to respond to changes or to take certain actions.

Covenants with our lenders require compliance with specific financial ratios that may make it difficult for us to obtain additional financing on acceptable terms for future acquisitions or other corporate needs. Oaktree agreed to forbear from taking any action, including acceleration of payment of the term loans, if we fail to satisfy these covenants in the fourth quarter of 2012 and for each quarter in 2013 in a forbearance and commitment letter dated March 11, 2013. Oaktree agreed to forbearance with respect to the secured leverage ratio, the total net debt leverage ratio, and minimum liquidity restrictions.

Although we anticipate meeting our covenants in the future, our ability to remain in compliance with the covenants may be adversely affected by future events potentially beyond our control. Violating any of these covenants could result in being declared in default, which may result in our lenders electing to declare our outstanding borrowings immediately due and payable and terminate all commitments to extend further credit. If the lenders accelerate the repayment of borrowings, we cannot provide assurance that we will have sufficient liquidity to repay our credit facilities or other indebtedness. In addition, certain domestic and international subsidiaries have pledged the shares of certain subsidiaries, as well as accounts receivable, inventory, machinery and equipment, intellectual property and other assets as collateral. If we default on our obligations, our lenders may take possession of the collateral and may license, sell or otherwise dispose of those related assets in order to satisfy our obligations. Refer to Note 6, Debt, to our Consolidated Financial Statements for additional discussion of our debt covenants.

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Our primary lender and investor, Oaktree Capital Management, may have interests that diverge from our interests and the interests of other security holders.

Oaktree Capital Management L.P. (“Oaktree”) and affiliates is our primary creditor and beneficially own a significant equity position in the Company. Oaktree may have interests that diverge from our interests and the interests of other security holders. In addition, so long as Oaktree maintains ownership at specified thresholds, it has the right to nominate up to three members of our board of directors and will be entitled to certain information rights and a right to participate in future offerings of our equity securities. Oaktree is in the business of investing in companies and is not restricted by contract from investing in our current or future competitors. Future events may give rise to a divergence of interests between Oaktree and us or our other security holders that would have a material adverse effect on our Company. Oaktree’s ownership and control may also have the effect of delaying or preventing a change of control, impeding a merger, consolidation, takeover or other business combination or discourage a potential acquirer from making a tender offer. Oaktree’s ownership and control may also limit our ability to issue stock, incur further debt, or dispose of any material assets of the Company or its subsidiaries.

Reduced prices for our products may adversely affect our profit margins if we are unable to reduce our cost structure.

The average selling prices for our products tend to decrease over their life cycle. In addition, foreign currency movements and the desire to retain market share increase the pressure on our customers to seek lower prices from their suppliers. As a result, our customers are likely to continue to demand lower prices from us. To maintain our margins and remain profitable, we must continue to meet our customers’ design needs while concurrently reducing costs through efficient raw material procurement, process and product improvements and reducing our operating expense levels. Our profit margins and cash flows may suffer if we are unable to reduce our overall cost structure relative to decreases in sales prices.

Rising raw material and production costs may decrease our gross margin.

We use commodities such as copper and plastic resins in manufacturing our products. Prices of these and other raw materials have experienced significant volatility in the past. Other manufacturing costs, such as direct and indirect labor, energy, freight and packaging costs, also directly impact the costs of our products. If we are unable to pass these increased costs to our customers or recover the increased costs through production efficiencies, our gross margins may suffer.

An inability to adequately respond to changes in technology, applicable standards or customer needs may decrease our sales.

We operate in an industry characterized by rapid change caused by the frequent emergence of new technologies and standards. Generally, we expect life cycles for products in the electronic components industry to be relatively short. This requires us to anticipate and respond rapidly to changes in industry standards and customer needs, and, also, to develop and introduce new and enhanced products on a timely and cost-effective basis. Our engineering and development teams place a priority on working closely with our customers to design innovative products and to improve our manufacturing processes. Improving performance and reducing costs for our customers requires the continual development of new products and/or improvement to the components of existing products. Our inability to react quickly and efficiently to changes in technology, standards or customer needs may decrease our sales or margins.

If our inventory becomes obsolete, then our future performance and operating results will be adversely affected.

The life cycles of our products depend heavily upon the life cycles of the end products for which our products are designed. End products with short life cycles require us to closely manage our production and inventory levels, as

adverse changes in end market demand may make our products obsolete. Specifically, during market slowdowns, this may result in significant charges for inventory write-offs. Our future operating results may be adversely affected by material levels of inventory reserves for obsolete or excess inventory.

Our decisions to strategically divest current businesses or our inability to capitalize on prior or future acquisitions may adversely affect our business.

We have completed numerous acquisitions and divestitures in the past and we may continue to seek acquisitions to grow our businesses. We may also divest operations to focus on our core businesses. We may fail to derive significant benefits from such transactions. Also, if we fail to achieve sufficient financial performance from an acquisition, certain long-lived assets, such as property, plant and equipment and intangible assets, could become impaired and result in the recognition of an impairment loss.

The success of our acquisitions depends on our ability to:

- successfully execute the integration or consolidation of the acquired operations into our existing businesses;
- develop or modify the financial reporting and information systems of the acquired entity to ensure overall financial integrity and adequacy of internal control procedures;
- identify and take advantage of cost reduction opportunities; and
- further penetrate existing markets with the product capabilities we may acquire.

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Integration of acquisitions may take longer than we expect and may never be achieved to the extent originally anticipated. This could result in lower than expected business growth or higher than anticipated costs. In addition, acquisitions may:

cause a disruption in our ongoing business;
distract our managers;
increase our debt and leverage;
unduly burden other resources in our company; and

result in an inability to maintain our historical standards, procedures and controls, which may result in non-compliance with external laws and regulations or contractual requirements.

Alternatively, we may also consider making strategic divestitures, which may also:

cause a disruption in our ongoing business;
distract our managers;
unduly burden other resources in our company; and

result in an inability to maintain our historical standards, procedures and controls, which may result in non-compliance with external laws and regulations or contractual requirements.

We may record impairment losses in the future. We assess the impairment of long-lived assets whenever events or changes in circumstances indicate an asset's carrying value may not be recoverable. Factors we consider important that could trigger an impairment review include significant changes in the use of any asset, changes in trends of historical operating performance, a significant decline in the price of our common stock, changes in projected operating performance and significant negative economic trends.

An inability to identify, consummate or integrate acquisitions or a lack of appropriate investment in capital expenditure and research, development and engineering may slow our future growth.

We may identify and possibly consummate acquisitions in the future to penetrate or expand important markets and to grow our business. We may not be able to identify suitable acquisition candidates at reasonable prices. Even if we identify promising acquisition candidates, the timing, price, structure and success of future acquisitions are uncertain. An inability to consummate or integrate attractive acquisitions may reduce our growth rate and our ability to penetrate new markets.

We remain committed to technological development through investing in research, development and engineering activities focused on designing next-generation products, improving our existing products and improving our manufacturing processes. If we determine that any of our manufacturing processes would benefit from capital investment, we may allocate resources to fund the expansion of property, plant and equipment used in these processes. An inability to allocate resources to the appropriate investment or an inability to allocate the appropriate amount of resources to an investment may reduce our ability to grow organically.

If any of our major customers terminates a substantial amount of existing agreements, chooses not to enter into new agreements or elects not to submit additional purchase orders for our products, then our business may suffer.

Our sales are predominantly made on a purchase order basis. We have a concentration of several primary customers that we rely on for a material amount of these purchase orders. To the extent we have agreements in place with these customers, most of these agreements are either short-term in nature or provide these customers with the ability to terminate the arrangement. Such agreements typically do not provide us with any material recourse in the event of non-renewal or early termination.

We will lose business and our revenues may decrease if one or more of these major customers:

does not submit additional purchase orders;
does not enter into new agreements with us;
elects to reduce or delay their purchase orders; or
elects to terminate their relationship with us.

If we do not effectively manage our business when facing fluctuations in the size of our organization, then our business may be disrupted.

We have changed our capacity as a result of declines in global demand and through divestitures. We may significantly reduce or expand our workforce and facilities in response to rapid changes in demand for our products due to prevailing global market conditions. These rapid fluctuations place strains on our resources and systems. If we do not effectively manage our resources and systems, our business may be adversely affected.

Uncertainty in demand for our products may adversely affect our results of operations and financial condition.

We have very little visibility into our customers' future purchasing patterns and are highly dependent on customer forecasts. However, these forecasts are non-binding and can often significantly change. Given the fluctuation in growth rates and the occasional cyclical nature of demand for our products, as well as our reliance on our customers' forecasts, it is difficult to accurately manage our production schedule, equipment and personnel needs, as well as our raw material and working capital requirements.

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Our failure to effectively manage these issues may result in:

production delays;
increased costs of production;
excessive inventory levels and reduced financial liquidity;
an inability to make timely deliveries; and
a decrease in profits or cash flows.

A decrease in the availability of our key raw materials could adversely affect our profit margins.

We use several types of raw materials in the manufacturing of our products, including:

base metals such as copper;
ferrite cores;
plastics and plastic resins; and
rare earth metals.

Some of these materials are only produced by a limited number of suppliers. The limited amount of suppliers may restrict our ability to obtain these raw materials in sufficient quantities, at reasonable prices or in a timely manner to meet customer demand for our products. A lack of availability or a delay in obtaining any of the raw materials used in our products could adversely affect our manufacturing costs and profit margins. In addition, if the price of our raw materials increases significantly over a short period of time due to increased market demand or shortage of supply, customers may be unwilling to bear the increased price for our products and we may be forced to sell our products containing these materials at lower prices causing a reduction in our profit margins.

Our operating results may be adversely affected by new regulations relating to the sourcing of certain raw materials.

Section 1502 of the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2012 (the Dodd-Frank Act), contains provisions to improve the transparency and accountability concerning the supply of minerals originating from the conflict zones of the Democratic Republic of Congo and adjoining countries. As a result, the SEC recently established new annual disclosure and reporting requirements for those companies who use “conflict” minerals mined from those countries in their products. When these new requirements are implemented, they could affect the sourcing and availability of minerals used in our manufacturing processes. As a result, we may not be able to obtain products at competitive prices and there may be additional costs associated with complying with the SEC’s new due diligence procedures and disclosure requirements. We may also encounter challenges to satisfy those customers who require that all of the components of our products are certified as conflict-free. If we are not able to meet customer requirements, customers may choose to disqualify us as a supplier.

Competition may result in reduced demand for our products and reduce our sales.

We operate in a highly competitive worldwide industry, with relatively low barriers to competitive entry. We frequently encounter strong competition within individual product lines from various competitors throughout the world, some of which are larger than us and have significantly greater financial resources and technological capabilities. We compete principally on the basis of:

engineering expertise;
product quality and reliability;
global design and manufacturing capabilities;
breadth of product line;

price;
customer service; and
delivery time.

Our inability to successfully compete on any or all of the above or other factors may result in reduced sales.

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

Despite our quality control and quality assurance efforts, defects may occur in the products we manufacture due to design or manufacturing errors or component failure. Product defects may result in delayed shipments and reduced demand for our products. We may be subject to increased costs due to warranty claims on defective products. We may be required to participate in a recall involving products which are, or are alleged to be, defective. We carry insurance for certain legal matters involving product liability; however, we do not have coverage for all costs related to product defects and the costs of such claims, including costs of defense and settlement, may exceed our available coverage.

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Fluctuations in foreign currency exchange rates may adversely affect our operating results.

We manufacture and sell our products in various regions of the world and export and import these products to and from a large number of countries. Fluctuations in exchange rates could negatively impact our cost of production and sales which, in turn, could decrease our operating results and cash flow. In addition, if the functional currency of our manufacturing costs strengthens as compared to the functional currency of our competitors' manufacturing costs, our products may become more costly than our competitors.

Our international operations subject us to the risks of unfavorable political, regulatory, labor and tax conditions in other countries.

We manufacture and assemble most of our products in locations outside the United States, primarily in the People's Republic of China ("PRC" or China), and a majority of our revenues are derived from sales to customers outside the United States. Our future operations and earnings may be adversely affected by the risks related to, or any other problems arising from, operating in international locations and markets.

Risks inherent in doing business internationally may include:

the inability to repatriate or transfer cash on a timely or efficient basis;
economic and political instability;
expropriation and nationalization;
trade restrictions;
capital and exchange control programs;
transportation delays;
uncertain rules of law; and

uncertain changes in the laws and policies of the United States or of the countries in which we manufacture and sell our products.

The majority of our manufacturing occurs in the PRC. Although the PRC has a large and growing economy, its political, legal and labor developments entail uncertainties and risks. For example, the availability of labor is highly seasonal and is significantly affected by the migration of workers in relation to the annual Lunar New Year holiday as well as economic conditions in the PRC. At certain times in the past we have encountered difficulties in attracting and retaining the level of labor required to meet our customers' demands. Also, wages and benefits have been increasing rapidly over the last several years in China. While China has been receptive to foreign investment, its investment policies may not continue indefinitely into the future and future policy changes may adversely affect our ability to conduct our operations in these countries or the costs of such operations.

We have benefited in prior years from favorable tax incentives and we operate in countries where we realize favorable income tax treatment relative to the U.S. statutory rate. We have been granted special tax incentives, including tax holidays, in jurisdictions such as the PRC. This favorable situation could change if these countries were to increase rates or discontinue the special tax incentives, or if we discontinue our manufacturing operations in any of these countries and do not replace them with operations in locations with similar tax incentives or policies. Accordingly, in the event of changes in laws and regulations affecting our international operations, we may not be able to continue to recognize or take advantage of similar benefits in the future.

We could be adversely affected by violations of the U.S. Foreign Corrupt Practices Act and similar worldwide anti-bribery laws.

The U.S. Foreign Corrupt Practices Act ("FCPA") and similar worldwide anti-bribery laws generally prohibit companies and their intermediaries from making improper payments to government officials for the purpose of obtaining or retaining business. Our policies mandate compliance with these anti-bribery laws. We operate in many parts of the world that have experienced governmental corruption to some degree, and in certain circumstances, strict compliance with anti-bribery laws may conflict with local customs and practices. Despite our training and compliance program, we cannot assure you that our internal control policies and procedures always will protect us from reckless or criminal acts committed by our employees or agents. Violations of these laws, or allegations of such violations, could disrupt our business and result in a material adverse effect on our results of operations, financial position, and cash flows.

Liquidity requirements could necessitate movements of existing cash balances, which may be subject to restrictions or may cause unfavorable tax and earnings consequences.

A significant portion of our cash is held offshore by international subsidiaries and may be denominated in currencies other than the U.S. dollar. While we intend to use a significant amount of the cash held overseas to fund our international operations and growth, if we encounter a significant need for liquidity domestically or at a particular location that we cannot fulfill through borrowings, equity offerings, or other internal or external sources, we may experience unfavorable tax and earnings consequences due to cash transfers. For example, these adverse consequences would occur if the transfer of cash into the United States is taxed with no available foreign tax credit to offset the U.S. tax liability, resulting in lower net earnings. Also, we may be prohibited or significantly delayed when transferring cash from a country such as the PRC, as there are foreign exchange ceilings imposed by local governments and often lengthy approval processes, which foreign governments require for international cash transfers. We have not experienced any significant liquidity restrictions in any of the countries in which we operate and we do not presently foresee any.

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At December 28, 2012, a majority owned foreign subsidiary and its subsidiaries held approximately \$11.6 million of our total consolidated cash and cash equivalents. Permanent access to funds from this subsidiary could be in the form of a dividend to its shareholders, which could result in income withholding taxes and distributions to minority shareholders. During fiscal 2012, this majority owned subsidiary declared a dividend of approximately \$7.0 million, which was paid in November 2012. Distributions to minority shareholders, withholding and other taxes reduced the net proceeds of the dividend to the Company to approximately \$4.8 million.

Losing the services of our executive officers or other highly qualified and experienced employees could adversely affect our businesses.

Our success depends upon the contributions of our executive officers and senior management, many of whom have numerous years of experience and would be extremely difficult to replace. We must also attract and maintain experienced and highly skilled engineering, sales and marketing, finance and manufacturing personnel. Competition for qualified personnel is often intense, and we may not be successful in hiring and retaining these people. If we lose the services of these key employees or cannot attract and retain other qualified personnel, our businesses could be adversely affected.

We face risks arising from the restructuring of our operations.

In the past, we have undertaken initiatives to restructure our business operations with the intention of improving utilization and realizing cost savings in the future. These initiatives have included changing the number and location of our production facilities, largely to align our capacity and infrastructure with current and anticipated customer demand. This alignment includes transferring programs from higher cost geographies to lower cost geographies. The process of restructuring entails, among other activities, moving production between facilities, closing facilities, reducing the level of staff, realigning our business processes and reorganizing our management.

We continuously evaluate our operations and cost structure relative to general economic conditions, market demands, tax rates, cost competitiveness and our geographic footprint as it relates to our customers' production requirements. As a result of this ongoing evaluation, we could initiate future restructuring plans. Restructurings present significant potential risks of events occurring that could adversely affect us, including a decrease in employee morale, delays encountered in finalizing the scope of, and implementing, the restructurings (including extensive consultations concerning potential workforce reductions, particularly in locations outside of the U.S.), the failure to achieve targeted cost savings and the failure to meet operational targets and customer requirements due to the loss of employees and any work stoppages that might occur. These risks are further complicated by our extensive international operations, which subject us to different legal and regulatory requirements that govern the extent and speed of our ability to reduce our manufacturing capacity and workforce. In addition, the current global economic conditions may change how governments regulate restructuring as the recent global recession has impacted local economies. Finally, we may have to obtain agreements from our affected customers for the relocation of our facilities in certain instances. Obtaining these agreements, along with the volatility in our customers' demand, can further delay restructuring activities.

Public health epidemics (such as flu strains or severe acute respiratory syndrome) or natural disasters (such as earthquakes or fires) may disrupt operations in affected regions and affect operating results.

We maintain extensive manufacturing operations in the PRC and elsewhere, similar to many of our customers and suppliers. A sustained interruption of our manufacturing operations or those of our customers or suppliers, resulting from complications caused by a public health epidemic or a natural disaster could have a material adverse effect on our business and our results of operations.

The unavailability of insurance against certain business and product liability risks may adversely affect our future operating results.

As part of our comprehensive risk management program, we purchase insurance coverage against certain business and product liability risks. However, not all risks are insurable and those that are insured may differ in the amount covered due to the type of risk, end market and customer location. If any of our insurance carriers discontinues an insurance policy, significantly reduces available coverage or increases our deductibles and we cannot find another insurance carrier to provide comparable coverage at similar costs or we are not fully insured for a particular risk in a particular place, then we may be subject to increased costs of uninsured or under-insured losses, which may adversely affect our operating results.

Also, our components, modules and other products are used in a broad array of representative end products. If our insurance program does not adequately cover liabilities arising from the direct use of our products or liabilities that arise from use of our customers' products, we may be subject to increased costs of uninsured losses, which may adversely affect our operating results.

Environmental liability and compliance obligations may adversely affect our operations and results.

Our manufacturing operations are subject to a variety of environmental laws and regulations, as well as internal programs and policies governing:

air emissions;
wastewater discharges;