

BENCHMARK ELECTRONICS INC
Form 10-Q
November 08, 2018

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

FORM 10 Q

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

For the quarterly period ended September 30, 2018

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

For the transition period from _____ to _____

Commission File Number: 1 10560

BENCHMARK ELECTRONICS, INC.

(Exact name of registrant as specified in its charter)

	Texas	74 2211011
--	--------------	-------------------

Edgar Filing: BENCHMARK ELECTRONICS INC - Form 10-Q

	(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
	4141 N. Scottsdale Road	85251
	Scottsdale, Arizona	(Zip Code)
	(Address of principal executive offices)	

(623) 300-7000

(Registrant's telephone number, including area code)

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

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

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

Large accelerated filer <input checked="" type="checkbox"/>	Accelerated filer <input type="checkbox"/>
Non-accelerated filer <input type="checkbox"/>	Smaller reporting company <input type="checkbox"/>
Emerging growth company <input type="checkbox"/>	

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

Edgar Filing: BENCHMARK ELECTRONICS INC - Form 10-Q

As of November 7, 2018, there were 43,710,356 shares of common stock of Benchmark Electronics, Inc., par value \$0.10 per share, outstanding.

TABLE OF CONTENTS

		Page
PART I—FINANCIAL INFORMATION		
<u>Item 1.</u>	<u>Financial Statements (Unaudited)</u>	1
	<u>Condensed Consolidated Balance Sheets</u>	1
	<u>Condensed Consolidated Statements of Income (Loss)</u>	2
	<u>Condensed Consolidated Statements of Comprehensive Income (Loss)</u>	3
	<u>Condensed Consolidated Statement of Shareholders' Equity</u>	4
	<u>Condensed Consolidated Statements of Cash Flows</u>	5
	<u>Notes to Condensed Consolidated Financial Statements</u>	6
<u>Item 2.</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	25
<u>Item 3.</u>	<u>Quantitative and Qualitative Disclosures About Market Risk</u>	34
<u>Item 4.</u>	<u>Controls and Procedures</u>	35
PART II—OTHER INFORMATION		
<u>Item 1.</u>	<u>Legal Proceedings</u>	36
<u>Item 1A.</u>	<u>Risk Factors</u>	36
<u>Item 2.</u>	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	36
<u>Item 6.</u>	<u>Exhibits</u>	37
<u>SIGNATURES</u>		38

PART I - FINANCIAL INFORMATION**Item 1. Financial Statements.****BENCHMARK ELECTRONICS, INC. AND SUBSIDIARIES****Condensed Consolidated Balance Sheets****(unaudited)**

(in thousands, except par value)	September 30, 2018	December 31, 2017 (as adjusted)
Assets		
Current assets:		
Cash and cash equivalents	\$ 475,713	\$ 742,546
Accounts receivable, net of allowance for doubtful accounts of \$1,729 and \$105, respectively	455,971	436,560
Contract assets	155,898	146,496
Inventories	321,194	268,917
Prepaid expenses and other assets	34,988	36,018
Income taxes receivable	38	120
Total current assets	1,443,802	1,630,657
Property, plant and equipment, net of accumulated depreciation of \$452,611 and \$432,043, respectively	208,495	186,473
Goodwill	192,116	191,616
Deferred income taxes	4,034	4,034
Other, net	92,324	96,524
	\$ 1,940,771	\$ 2,109,304
Liabilities and Shareholders' Equity		
Current liabilities:		
Current installments of long-term debt and capital lease obligations	\$ 4,880	\$ 18,274
Accounts payable	373,879	362,701
Income taxes payable	6,438	11,663
Accrued liabilities	92,976	85,679
Total current liabilities	478,173	478,317
Long-term debt and capital lease obligations, less current installments	149,341	193,406
Other long-term liabilities	90,615	89,749
Deferred income taxes	20,960	8,694
Shareholders' equity:		
Preferred stock, \$0.10 par value; 5,000 shares authorized, none issued	—	—
Common stock, \$0.10 par value; 145,000 shares authorized; issued		

Edgar Filing: BENCHMARK ELECTRONICS INC - Form 10-Q

and outstanding – 45,130 and 49,143, respectively	4,513	4,914
Additional paid-in capital	596,110	634,192
Retained earnings	609,577	708,181
Accumulated other comprehensive loss	(8,518)	(8,149)
Total shareholders' equity	1,201,682	1,339,138
Commitments and contingencies		
	\$ 1,940,771	\$ 2,109,304

See accompanying notes to condensed consolidated financial statements.

BENCHMARK ELECTRONICS, INC. AND SUBSIDIARIES**Condensed Consolidated Statements of Income (Loss)****(unaudited)**

(in thousands, except per share data)	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2018	2017	2018	2017
		(as adjusted)		(as adjusted)
Sales	\$ 640,688	\$ 610,929	\$ 1,909,415	\$ 1,788,443
Cost of sales	587,911	552,686	1,744,021	1,623,184
Gross profit	52,777	58,243	165,394	165,259
Selling, general and administrative expenses	37,607	32,093	109,182	97,079
Amortization of intangible assets	2,368	2,736	7,101	7,698
Restructuring charges and other costs	1,845	2,511	5,838	5,566
Income from operations	10,957	20,903	43,273	54,916
Interest expense	(3,822)	(2,324)	(8,543)	(6,861)
Interest income	1,619	1,334	5,197	3,621
Other income (expense)	1,139	(394)	827	(1,305)
Income before income taxes	9,893	19,519	40,754	50,371
Income tax expense	2,094	1,688	45,653	5,911
Net income (loss)	\$ 7,799	\$ 17,831	\$ (4,899)	\$ 44,460
Earnings (loss) per share:				
Basic	\$ 0.17	\$ 0.36	\$ (0.10)	\$ 0.89
Diluted	\$ 0.17	\$ 0.35	\$ (0.10)	\$ 0.88
Weighted-average number of shares outstanding:				
Basic	46,301	49,865	47,415	49,716
Diluted	46,455	50,330	47,415	50,292

See accompanying notes to condensed consolidated financial statements.

BENCHMARK ELECTRONICS, INC. AND SUBSIDIARIES**Condensed Consolidated Statements of Comprehensive Income (Loss)****(unaudited)**

(in thousands)	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2018	2017	2018	2017
		(as adjusted)		(as adjusted)
Net income (loss)	\$ 7,799	\$ 17,831	\$ (4,899)	\$ 44,460
Other comprehensive income (loss):				
Foreign currency translation adjustments	(249)	1,313	(1,569)	4,434
Unrealized gain on investments, net of tax	—	3	41	19
Unrealized gain on derivative, net of tax	82	89	1,159	254
Other	—	—	—	(13)
Other comprehensive income (loss)	(167)	1,405	(369)	4,694
Comprehensive income (loss)	\$ 7,632	\$ 19,236	\$ (5,268)	\$ 49,154

See accompanying notes to condensed consolidated financial statements.

BENCHMARK ELECTRONICS, INC. AND SUBSIDIARIES**Condensed Consolidated Statement of Shareholders' Equity****(unaudited)**

(in thousands)	Common Stock Shares Outstanding	Common Stock Par Value	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total Shareholders' Equity
Balances, December 31, 2017 (as adjusted)	49,143	\$ 4,914	\$ 634,192	\$ 708,181	\$ (8,149)	\$ 1,339,138
Stock-based compensation expense	—	—	8,229	—	—	8,229
Shares repurchased and retired	(4,401)	(440)	(48,913)	(72,700)	—	(122,053)
Stock options exercised	187	19	3,444	—	—	3,463
Vesting of restricted stock units	229	23	(23)	—	—	—
Shares withheld for taxes	(28)	(3)	(819)	—	—	(822)
Dividends declared	—	—	—	(21,005)	—	(21,005)
Net loss	—	—	—	(4,899)	—	(4,899)
Other comprehensive loss	—	—	—	—	(369)	(369)
Balances, September 30, 2018	45,130	\$ 4,513	\$ 596,110	\$ 609,577	\$ (8,518)	\$ 1,201,682

See accompanying notes to condensed consolidated financial statements.

BENCHMARK ELECTRONICS, INC. AND SUBSIDIARIES**Condensed Consolidated Statements of Cash Flows****(unaudited)**

(in thousands)	Nine Months Ended September 30,	
	2018	2017 (as adjusted)
Cash flows from operating activities:		
Net income (loss)	\$ (4,899)	\$ 44,460
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation	29,104	27,452
Amortization	10,539	9,139
Provision for doubtful accounts	1,714	1,697
Deferred income taxes	11,863	581
Gain on the sale of property, plant and equipment	(215)	(194)
Asset impairments	96	42
Stock-based compensation expense	8,229	6,819
Changes in operating assets and liabilities, net of effects from business acquisition:		
Accounts receivable	(21,733)	29,229
Contract assets	(9,402)	(5,373)
Inventories	(54,342)	(36,747)
Prepaid expenses and other assets	2,493	(8,181)
Accounts payable	12,620	3,922
Accrued liabilities	2,170	15,637
Income taxes	(5,530)	1,407
Net cash provided by (used in) operations	(17,293)	89,890
Cash flows from investing activities:		
Proceeds from sales of investments at par	522	250
Additions to property, plant and equipment	(50,437)	(35,033)
Proceeds from the sale of property, plant and equipment	237	270
Additions to purchased software	(2,496)	(2,703)
Business acquisition, net of cash acquired	(2,731)	—
Other	(130)	(156)
Net cash used in investing activities	(55,035)	(37,372)
Cash flows from financing activities:		
Proceeds from stock options exercised	3,463	9,828
Employee taxes paid for shares withheld	(822)	(383)
Dividends paid	(14,235)	—
Borrowings under credit agreement	50,000	—
Principal payments on long-term debt and capital lease obligations	(107,758)	(9,288)

Edgar Filing: BENCHMARK ELECTRONICS INC - Form 10-Q

Share repurchases	(122,053)	(5,887)
Debt issuance costs	(2,303)	(433)
Net cash used in financing activities	(193,708)	(6,163)
Effect of exchange rate changes	(797)	2,358
Net increase (decrease) in cash and cash equivalents	(266,833)	48,713
Cash and cash equivalents at beginning of year	742,546	681,433
Cash and cash equivalents at end of period	\$ 475,713	\$ 730,146

See accompanying notes to condensed consolidated financial statements.

BENCHMARK ELECTRONICS, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(amounts in thousands, except per share data, unless otherwise noted)

(unaudited)

Note 1 – Basis of Presentation

Benchmark Electronics, Inc. (the Company) is a Texas corporation that provides innovative product design, engineering services, technology solutions and advanced manufacturing services. From initial product concept to volume production, including direct order fulfillment and aftermarket services, the Company has been providing integrated services and solutions to original equipment manufacturers (OEMs) since 1979. The Company serves the following industries: aerospace and defense (A&D), medical technologies, complex industrials, test and instrumentation, next-generation telecommunications and high-end computing. The Company has manufacturing operations located in the United States and Mexico (the Americas), Asia and Europe.

The unaudited condensed consolidated financial statements included herein have been prepared by the Company pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC). The financial statements reflect all normal and recurring adjustments necessary in the opinion of management for a fair presentation of the financial position, results of operations and cash flows for the interim periods presented. The results of operations for the periods presented are not necessarily indicative of the results to be expected for the full year. The accompanying unaudited condensed consolidated financial statements should be read in conjunction with the financial statements and notes included in the Company's annual report on Form 10-K for the year ended December 31, 2017 (the 2017 10-K).

Management has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements in accordance with generally accepted accounting principles in the United States (U.S. GAAP). Actual results could differ from those estimates and assumptions.

Note 2 – New Accounting Pronouncements

Adopted in 2018

In May 2017, the Financial Accounting Standards Board (FASB) issued a new accounting standards update that provides guidance about which changes to the terms or conditions of a share-based payment award require an entity to apply modification accounting. The Company adopted the new guidance effective January 1, 2018. The impact of adoption on the Company's consolidated financial statements is dependent on future changes to stock-based compensation awards.

In August 2016, the FASB issued a new accounting standards update, which seeks to reduce the existing diversity in how certain cash receipts and cash payments are presented and classified in the statement of cash flows. The Company adopted this new update effective January 1, 2018. The adoption of this guidance had no impact on the consolidated financial statements of the Company.

In May 2014, the FASB issued a new standard (commonly referred to as ASC 606), which changed the way the Company recognizes revenue and significantly expanded the disclosure requirements for revenue arrangements. The Company adopted ASC 606 with a date of the initial application of January 1, 2018. As a result, the Company has changed its accounting policy for revenue recognition as detailed below.

The Company applied ASC 606 using the full retrospective transition method. The Company elected the ASC 606 practical expedient and does not disclose the information about remaining performance obligations that have original expected durations of one year or less. Amounts prior to January 1, 2018 that have been adjusted in accordance with ASC 606 as described herein are noted “as adjusted”.

Previously, the Company recognized revenue from the sale of manufactured products built to customer specifications and excess inventory when title and risk of ownership passed, the price to the buyer was fixed or determinable and recoverability was reasonably assured, which was generally when the goods were shipped. Under ASC 606, the Company recognizes revenue as the customer takes control of the products. Under the majority of the Company's manufacturing contracts with customers, the customer controls all of the work-in-progress as products are being built. Revenues under these contracts are recognized progressively based on the cost-to-cost method. Accordingly, the Company will recognize revenue under these contracts earlier than under the previous accounting rules. Under other manufacturing contracts, the customer does not take control of the product until it is completed. Under these contracts, the Company continues to recognize revenue upon transfer of control of product to the customer. Revenue from design, development and engineering services also continues to be recognized over time as the services are performed.

The Company's performance obligations generally have an expected duration of one year or less. The Company applies the practical expedients and does not disclose information about remaining performance obligations that have original expected durations of one year or less or any significant financing components in the contracts.

The Company recognizes the incremental costs, if any, of obtaining contracts as an expense when incurred since the amortization period of the assets that the Company otherwise would have recognized is one year less.

The following tables summarize the impacts of ASC 606 adoption on the Company's 2017 consolidated financial statements.

Condensed Consolidated Balance Sheet December 31, 2017

(in thousands)	Impact of changes in accounting policies		
	As previously reported	Adjustments	As adjusted
Contract assets	\$ —	\$ 146,496	\$ 146,496
Inventories	397,181	(128,264)	268,917
Prepaid expenses and other assets	42,263	(6,245)	36,018
Total assets	\$ 2,097,317	\$ 11,987	\$ 2,109,304
Income taxes payable	\$ 11,662	\$ 1	\$ 11,663
Deferred income taxes	7,027	1,667	8,694
Total liabilities	768,498	1,668	770,166
Retained earnings	697,862	10,319	708,181
Total shareholders' equity	1,328,819	10,319	1,339,138
Total liabilities and shareholders' equity	\$ 2,097,317	\$ 11,987	\$ 2,109,304

**Condensed Consolidated Statement of Income
Three Months Ended September 30, 2017**

(in thousands, except per share data)	Impact of changes in accounting policies		
	As previously reported	Adjustments	As adjusted
Sales	\$ 603,550	\$ 7,379	\$ 610,929
Cost of sales	\$ 545,395	\$ 7,291	\$ 552,686
Income tax expense	\$ 1,919	\$ (231)	\$ 1,688
Net income	\$ 17,512	\$ 319	\$ 17,831
Earnings per share:			
Basic	\$ 0.35	\$ 0.01	\$ 0.36
Diluted	\$ 0.35	\$ —	\$ 0.35
Weighted-average number of shares outstanding:			
Basic	49,865	49,865	49,865
Diluted	50,330	50,330	50,330

**Condensed Consolidated Statement of Income
Nine Months Ended September 30, 2017**

(in thousands, except per share data)	Impact of changes in accounting policies		
	As previously reported	Adjustments	As adjusted
Sales	\$ 1,786,955	\$ 1,488	\$ 1,788,443
Cost of sales	\$ 1,621,153	\$ 2,031	\$ 1,623,184
Income tax expense	\$ 6,539	\$ (628)	\$ 5,911
Net income	\$ 44,375	\$ 85	\$ 44,460
Earnings per share:			
Basic	\$ 0.89	\$ —	\$ 0.89
Diluted	\$ 0.88	\$ —	\$ 0.88
Weighted-average number of shares outstanding:			
Basic	49,716	49,716	49,716
Diluted	50,292	50,292	50,292

Condensed Consolidated Statement of Cash Flows
Nine Months Ended September 30, 2017

(in thousands)	Impact of changes in accounting policies		
	As previously reported	Adjustments	As adjusted
Net income	\$ 44,375	\$ 85	\$ 44,460
Adjustments to reconcile net income to net cash provided			
by operating activities:			
Depreciation	27,452	—	27,452
Amortization	9,139	—	9,139
Provision for doubtful accounts	1,697	—	1,697
Deferred income taxes	1,505	(924)	581
Gain on the sale of property, plant and equipment	(194)	—	(194)
Asset impairments	42	—	42
Stock-based compensation expense	6,819	—	6,819
Changes in operating assets and liabilities:			
Accounts receivable	29,229	—	29,229
Contract assets	—	(5,373)	(5,373)
Inventories	(38,778)	2,031	(36,747)
Prepaid expenses and other assets	(12,066)	3,885	(8,181)
Accounts payable	3,922	—	3,922
Accrued liabilities	15,637	—	15,637
Income taxes	1,111	296	1,407
Net cash provided by operations	89,890	—	89,890
Net cash used in investing activities	(37,372)	—	(37,372)
Net cash used in financing activities	(6,163)	—	(6,163)
Effect of exchange rate changes	2,358	—	2,358
Net increase in cash and cash equivalents	48,713	—	48,713
Cash and cash equivalents at beginning of year	681,433	—	681,433
Cash and cash equivalents at end of period	\$ 730,146	\$ —	\$ 730,146

Not Yet Adopted

In February 2018, the FASB issued optional new accounting guidance that allows the reclassification of certain tax effects from accumulated other comprehensive income to retained earnings. This guidance is effective January 1, 2019, with early adoption permitted. The Company is evaluating whether it will adopt this new guidance along with any impacts on the Company's financial position, results of operations and cash flows, none of which are expected to be material.

In June 2016, the FASB issued a new accounting standards update, which replaces the current incurred loss impairment methodology with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. This update is effective for annual reporting periods beginning after December 15, 2019. The Company does not expect the implementation of this update to have a material impact on its consolidated financial position, results of operations or cash flows; and will adopt this update effective January 1, 2020.

In February 2016, the FASB issued a new accounting standards update changing the accounting for leases, including a requirement to record all leases on the consolidated balance sheets as assets (right-of-use) and

liabilities (for reasonably certain lease payments). This update is effective for fiscal years beginning after December 15, 2018. The Company will adopt this update effective January 1, 2019, which will impact its consolidated balance sheet. Originally, entities were required to adopt this update using a modified retrospective approach, which required prior periods to be presented under this new standard with various practical expedients allowed. However, in July 2018, the FASB issued additional guidance which allows entities the option of recognizing the cumulative effect of applying the new standard as an adjustment to the opening balance of retained earnings in the year of adoption (January 1, 2019). The Company is currently evaluating the impact this standard will have on its consolidated financial statements and which transition approach will be used upon adoption.

The Company has determined that other recently issued accounting standards will either have no material impact on its consolidated financial position, results of operations or cash flows, or will not apply to its operations.

Note 3 – Revenue

The Company's revenues are generated primarily from the sale of manufactured products built to customer specifications. The Company also generates revenue from design, development and engineering services, in addition to the sale of excess inventory.

Revenue is measured based on a consideration specified in a contract with a customer. The Company recognizes revenue when it satisfies a performance obligation by transferring control over a manufactured product to a customer. The Company's contracts with customers are generally short-term in nature. Customers are generally billed when the product is shipped or as services are performed. Under the majority of the Company's manufacturing contracts with customers, the customer controls all of the work-in-progress as products are being built. Revenues under these contracts are recognized progressively based on the cost-to-cost method. For other manufacturing contracts, the customer does not take control of the product until it is completed. Under these contracts, the Company recognizes revenue upon transfer of control of product to the customer. Revenue from design, development and engineering services is recognized over time as the services are performed. The Company assumes no significant obligations after shipment as it typically warrants workmanship only. Therefore, the warranty provisions are generally not significant.

If the Company records revenue, but does not issue an invoice, a contract asset is recognized. The contract asset is transferred to accounts receivable when the entitlement to payment becomes unconditional.

Taxes assessed by governmental authorities that are both imposed on and concurrent with a specific revenue-producing transaction, that are collected by the Company from a customer, are excluded from revenue.

Shipping and handling costs associated with outbound freight after control over a product has transferred to a customer are accounted for as fulfillment costs and are included in cost of sales.

Disaggregation of revenue

In the following tables, revenue is disaggregated by market sector. The tables also include a reconciliation of the disaggregated revenue with the reportable operating segments.

Reportable Operating Segments				
Three Months Ended September 30, 2018				
(in thousands)	Americas	Asia	Europe	Total
Market Sector:				
Industrials	\$ 45,334	\$ 67,969	\$ 15,001	\$ 128,304
A&D	97,141	—	7,847	104,988
Medical	58,725	34,404	3,171	96,300
Test and instrumentation	32,016	30,494	14,098	76,608
Computing	125,110	18,018	2,258	145,386
Telecommunication	37,846	50,716	540	89,102
External revenue	396,172	201,601	42,915	640,688
Elimination of intersegment sales	7,965	8,552	139	16,656
Segment revenue	\$ 404,137	\$ 210,153	\$ 43,054	\$ 657,344

Reportable Operating Segments				
Nine Months Ended September 30, 2018				
(in thousands)	Americas	Asia	Europe	Total
Market Sector:				
Industrials	\$ 141,966	\$ 180,195	\$ 49,887	\$ 372,048
A&D	278,191	—	23,093	301,284
Medical	173,192	106,769	10,142	290,103
Test and instrumentation	125,603	111,280	48,393	285,276
Computing	352,747	50,446	6,368	409,561
Telecommunication	123,386	125,708	2,049	251,143
External revenue	1,195,085	574,398	139,932	1,909,415
Elimination of intersegment sales	22,115	28,505	273	50,893
Segment revenue	\$ 1,217,200	\$ 602,903	\$ 140,205	\$ 1,960,308

Reportable Operating Segments				
Three Months Ended September 30, 2017 (as adjusted)				
(in thousands)	Americas	Asia	Europe	Total
Market Sector:				
Industrials	\$ 50,644	\$ 58,488	\$ 16,809	\$ 125,941
A&D	89,261	871	6,163	96,295
Medical	55,162	41,716	5,178	102,056
Test and instrumentation	42,587	34,071	12,454	89,112
Computing	96,688	26,257	2,396	125,341
Telecommunication	37,555	33,857	772	72,184
External revenue	371,897	195,260	43,772	610,929
Elimination of intersegment sales	7,520	12,947	54	20,521

Edgar Filing: BENCHMARK ELECTRONICS INC - Form 10-Q

Segment revenue \$ 379,417 \$ 208,207 \$ 43,826 \$ 631,450

Nine Months Ended September 30, 2017 (as adjusted)

Americas Asia Europe Total

Market Sector:

Industrials	\$ 160,794	\$ 156,373	\$ 50,714	\$ 367,881
A&D	275,717	1,920	18,638	296,275
Medical	150,902	108,015	14,899	273,816
Test and instrumentation	113,007	107,420	33,251	253,678
Computing	291,048	68,989	7,794	367,831
Telecommunication	130,708	96,243	2,011	228,962
External revenue	1,122,176	538,960	127,307	1,788,443
Elimination of intersegment sales	23,995	43,031	173	67,199
Segment revenue	\$ 1,146,171	\$ 581,991	\$ 127,480	\$ 1,855,642

11

For both the nine months ended September 30, 2018 and 2017, 93% of the Company's revenue was recognized as products and services are transferred over time.

Note 4 – Stock-Based Compensation

The Company's 2010 Omnibus Incentive Compensation Plan (the 2010 Plan) authorizes the Company, upon approval of the Compensation Committee of the Board of Directors, to grant a variety of awards, including stock options, restricted shares and restricted stock units (both time-based and performance-based) and other forms of equity awards, or any combination thereof, to any director, officer, employee or consultant (including any prospective director, officer, employee or consultant) of the Company. Stock options (which have not been awarded since 2015) are granted to employees with an exercise price equal to the market price of the Company's common stock on the date of grant, generally vest over a four-year period from the date of grant and have a term of 10 years. Time-based restricted stock units granted to employees generally vest over a four-year period from the date of grant, subject to the continued employment of the employee by the Company. Performance-based restricted stock units generally vest over a three-year performance cycle, which includes the year of the grant, and are based upon the Company's achievement of specified performance metrics. Awards under the 2010 Plan to non-employee directors have been in the form of restricted stock units, which vest in equal quarterly installments over a one-year period, starting on the grant date.

As of September 30, 2018, 2.7 million additional shares of common stock were available for issuance under the Company's 2010 Plan.

All share-based payments to employees, including grants of employee stock options, are recognized in the financial statements based on their grant date fair values. The total compensation cost recognized for stock-based awards was \$2.8 million and \$8.2 million for the three and nine months ended September 30, 2018, respectively, and \$2.3 million and \$6.8 million for the three and nine months ended September 30, 2017, respectively. The total income tax benefit recognized in the condensed income statements for stock-based awards was \$0.7 million and \$2.0 million for the three and nine months ended September 30, 2018, respectively, and \$0.8 million and \$2.5 million for the three and nine months ended September 30, 2017, respectively. The compensation expense for stock-based awards is recognized over the vesting period of the awards using the straight-line method. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model. Awards of restricted stock units and performance-based restricted stock units are valued at the closing market price of the Company's common stock on the date of grant. For performance-based restricted stock units, compensation expense is based on the probability that the performance goals will be achieved, which is monitored by management throughout the requisite service period. When it becomes probable, based on the Company's expectation of performance during the

measurement period, that more or less than the previous estimate of the awarded shares will vest, an adjustment to stock-based compensation expense is recognized as a change in accounting estimate.

As of September 30, 2018, the unrecognized compensation cost and remaining weighted-average amortization related to stock-based awards were as follows:

(in thousands, except remaining period data)	Stock Options	Time-based Restricted Stock Units	Performance- based Restricted Stock Units⁽¹⁾
Unrecognized compensation cost	\$ 112	\$ 15,143	\$ 4,315
Remaining weighted-average amortization period	0.4 years	2.4 years	1.4 years

⁽¹⁾ Based on the probable achievement of the performance goals identified in each award.

The total cash received by the Company as a result of stock option exercises for the nine months ended September 30, 2018 and 2017 was approximately \$3.5 million and \$9.8 million, respectively. The actual tax benefit realized as a result of stock option exercises and the vesting of other share-based awards during the nine months ended September 30, 2018 and 2017 was \$2.1 million and \$4.4 million, respectively. For the nine months ended September 30, 2018 and 2017, the total intrinsic value of stock options exercised was \$2.2 million and \$6.5 million, respectively.

The Company awarded performance-based restricted stock units to employees during the nine months ended September 30, 2018 and 2017. The number of performance-based restricted stock units that will ultimately be earned will not be determined until the end of the corresponding performance periods, and may vary from as low as zero to as high as 2.5 times the target number depending on the level of achievement of certain performance goals. The level of achievement of these goals is based upon the financial results of the Company for the last full calendar year within the performance period. The performance goals consist of certain levels of achievement using the following financial metrics: revenue growth, operating margin expansion, and return on invested capital. If the performance goals are not met based on the Company's financial results, the applicable performance-based restricted stock units will not vest and will be forfeited. Shares subject to forfeited performance-based restricted stock units will be available for issuance under the Company's 2010 Plan.

The following table summarizes activities relating to the Company's stock options:

	Number of Options (in thousands)	Weighted- Average Exercise Price	Weighted- Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value (in thousands)
Outstanding as of December 31, 2017	596	\$19.72		

Edgar Filing: BENCHMARK ELECTRONICS INC - Form 10-Q

Exercised	(187)	18.61		
Forfeited or expired	(20)	22.98		
Outstanding as of September 30, 2018	389	\$20.09	4.48	\$ 1,288
Exercisable as of September 30, 2018	354	\$19.78	3.51	\$ 1,279

The aggregate intrinsic value in the table above is before income taxes and is calculated as the difference between the exercise price of the underlying options and the Company's closing stock price as of the last

business day of the period ended September 30, 2018 for options that had exercise prices that were below the closing price.

The following table summarizes the activities related to the Company's time-based restricted stock units:

	Number of Units (in thousands)	Weighted- Average Grant Date Fair Value
Non-vested units outstanding as of December 31, 2017	593	\$27.47
Granted	402	29.52
Vested	(229)	26.79
Forfeited	(86)	27.35
Non-vested units outstanding as of September 30, 2018	680	\$28.93

The following table summarizes the activities related to the Company's performance-based restricted stock units:

	Number of Units (in thousands)	Weighted- Average Grant Date Fair Value
Non-vested units outstanding as of December 31, 2017	346	\$26.88
Granted ⁽¹⁾	120	29.60
Forfeited	(147)	24.06
Non-vested units outstanding as of September 30, 2018	319	\$29.19

⁽¹⁾ Represents target number of units that can vest based on the achievement of the performance goals.

Note 5 – Earnings Per Share

Basic earnings per share is computed using the weighted-average number of shares outstanding. Diluted earnings per share is computed using the weighted-average number of shares outstanding adjusted for the incremental shares attributed to outstanding stock equivalents. Stock equivalents include common stock issuable upon the exercise of stock options and other equity instruments, and are computed using the treasury stock method. Under the treasury stock method, the exercise price of a share and the amount of compensation cost, if any, for future service that the Company has not yet recognized are assumed to be used to repurchase shares in the current period.

The following table sets forth the calculation of basic and diluted earnings per share:

(in thousands, except per share data)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
		(as adjusted)		(as adjusted)
Net income (loss)	\$ 7,799	\$ 17,831	\$ (4,899)	\$ 44,460
Denominator for basic earnings per share - weighted-average number of common shares outstanding during the period	46,301	49,865	47,415	49,716
Incremental common shares attributable to exercise of dilutive options	90	268	—	319
Incremental common shares attributable to outstanding restricted stock units	64	197	—	257
Denominator for diluted earnings per share	46,455	50,330	47,415	50,292
Basic earnings (loss) per share	\$ 0.17	\$ 0.36	\$ (0.10)	\$ 0.89
Diluted earnings (loss) per share	\$ 0.17	\$ 0.35	\$ (0.10)	\$ 0.88

Potentially dilutive securities totaling 0.3 million common shares for the nine months ended September 30, 2018 were not included in the computation of diluted loss per share because their effect would have decreased the loss per share.

Note 6 – Goodwill and Other Intangible Assets

Goodwill allocated to the Company's reportable segments was as follows:

(in thousands)	Americas	Asia	Total
Goodwill as of December 31, 2017	\$ 153,514	\$ 38,102	\$ 191,616
Acquisition	500	—	500
Goodwill as of September 30, 2018	\$ 154,014	\$ 38,102	\$ 192,116

During the nine months ended September 30, 2018, the Company completed a non-significant business acquisition for \$2.7 million. The preliminary allocation of the net purchase price resulted in \$0.5 million of goodwill. The goodwill recognized in connection with the acquisition represents the future economic benefit arising from assets acquired that could not be individually identified and separately recognized, and is attributable to the general reputation, acquisition synergies and expected future cash flows of the acquisition. The final allocation of the purchase price, which the Company expects to complete no later than one year from the acquisition date, may differ from the amounts included in these financial statements.

Management does not expect additional adjustments, if any, resulting from changes to the purchase price allocation, to have a material effect on the Company's financial position or results of operations.

Other assets consist primarily of acquired identifiable intangible assets and capitalized purchased software costs. Intangible assets as of September 30, 2018 and December 31, 2017 were as follows:

(in thousands)	As of September 30, 2018		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Customer relationships	\$ 100,162	\$ (39,091)	\$ 61,071
Purchased software costs	37,645	(30,268)	7,377
Technology licenses	28,800	(20,214)	8,586
Trade names and trademarks	7,800	—	7,800
Other	868	(279)	589
Total	\$ 175,275	\$ (89,852)	\$ 85,423

(in thousands)	As of December 31, 2017		
	Gross Carrying Amount	Accumulated Amortization	Net Carrying Amount
Customer relationships	\$ 100,200	\$ (34,372)	\$ 65,828
Purchased software costs	35,328	(29,612)	5,716
Technology licenses	28,800	(17,887)	10,913
Trade names and trademarks	7,800	—	7,800
Other	868	(261)	607
Total	\$ 172,996	\$ (82,132)	\$ 90,864

Customer relationships are being amortized on a straight-line basis over a period of 10 to 14 years. Capitalized purchased software costs are being amortized on a straight-line basis over the estimated useful life of the related software, which ranges from 2 to 10 years. Technology licenses are being amortized over their estimated useful lives in proportion to the economic benefits consumed. The Company's acquired trade names and trademarks have been determined to have an indefinite life. Amortization for the nine months ended September 30, 2018 and 2017 was as follows:

(in thousands)	Nine Months Ended September 30,	
	2018	2017
Amortization of intangible assets	\$ 7,101	\$ 7,698
Amortization of capitalized purchased software costs	836	798
Amortization of debt costs	2,602	643
	\$ 10,539	\$ 9,139

The estimated future amortization expense of acquired intangible assets for each of the next five years is as follows (in thousands):

Year ending December 31,	Amount
2018 (remaining three months)	\$ 2,688
2019	10,653
2020	9,912
2021	6,868
2022	6,762

Note 7 – Borrowing Facilities

On July 20, 2018, the Company entered into a \$650 million credit agreement (the Credit Agreement) by and among the Company, certain of its subsidiaries, the lenders party thereto and Bank of America, N.A., as Administrative Agent, Swingline Lender and a L/C Issuer. The Credit Agreement is comprised of a five-year \$500 million revolving credit facility (the Revolving Credit Facility) and a five-year \$150 million term loan facility (the Term Loan Facility), both with a maturity date of July 20, 2023. The Term Loan Facility proceeds were used to (i) refinance a portion of existing indebtedness and terminate all commitments under the Company’s prior \$430 million Credit Agreement and (ii) pay the fees, costs and expenses associated with the foregoing and the negotiation, execution and delivery of the Credit Agreement.

The Revolving Credit Facility is available for general corporate purposes. The Credit Agreement includes an accordion feature pursuant to which the Company is permitted to add one or more incremental term loan and/or increase commitments under the Revolving Credit Facility in an aggregate amount not exceeding \$275 million, subject to the satisfaction of certain conditions.

The Term Loan Facility is payable in quarterly principal installments of \$1.9 million commencing June 30, 2019, with the balance payable on July 20, 2023.

Interest on outstanding borrowings under the Credit Agreement (other than swingline loans) accrues, at the Company’s option, at (a) the London Interbank Offered Rate (LIBOR) plus 1.0% to 2.0% or (b) the base rate plus 0.0% to 1.0%.

As of September 30, 2018, \$145.5 million of the outstanding debt under the Credit Agreement is effectively at a fixed interest rate as a result of a \$145.5 million notional interest rate swap contract discussed in Note 16. A commitment fee of 0.20% to 0.30% per annum (based on the debt to EBITDA ratio) on the unused portion of the revolving credit line is payable quarterly in arrears.

The Credit Agreement is generally secured by a pledge of (a) all the capital stock of the Company's domestic subsidiaries and 65% of the capital stock of its directly owned foreign subsidiaries, (b) all or substantially all other personal property of Benchmark and its domestic subsidiaries (including, but not limited to, accounts receivable, contract assets, inventory, intellectual property and fixed assets of Benchmark and its domestic subsidiaries), in each case, subject to customary exceptions and limitations, and (c) all proceeds and products of the property and assets described in (a) and (b) above.

The Credit Agreement contains certain financial covenants as to interest coverage and debt leverage, and certain customary affirmative and negative covenants, including restrictions on the Company's ability to incur additional debt and liens, pay dividends, repurchase shares, sell assets and merge or consolidate with other persons. Amounts due under the Credit Agreement could be accelerated upon specified events of default, including a failure to pay amounts due, breach of a covenant, material inaccuracy of a representation, or occurrence of bankruptcy or insolvency, subject, in some cases, to cure periods. As of

September 30, 2018, the Company was in compliance with all of these covenants and restrictions.

As of September 30, 2018, the Company had \$150.0 million in borrowings outstanding under the Term Loan facility and \$2.8 million in letters of credit outstanding under the Revolving Credit Facility. The Company had \$497.2 million available for future borrowings under the Revolving Credit Facility.

The Company's Thailand subsidiary has a multi-purpose credit facility with Kasikornbank Public Company Limited (the Thai Credit Facility) that provides for 350 million Thai baht (approximately \$10.8 million) working capital availability. The Thai Credit Facility is secured by land and buildings in Thailand owned by the Company's Thailand subsidiary. Availability of funds under the Thai Credit Facility is reviewed annually and is currently accessible through October 2019. As of both September 30, 2018 and December 31, 2017, there were no working capital borrowings outstanding under the facility.

Note 8 -Contract Assets

As of September 30, 2018 and December 31, 2017, the Company had \$155.9 million and \$146.5 million, respectively, in contract receivables from contracts with customers. The contract receivables primarily relate to the Company's right to consideration for work completed but not billed at the reporting date. The contract receivables are transferred to accounts receivable when the rights become unconditional.

Significant changes in the contract asset balance during the period are as follows:

(in thousands)	Nine Months Ended September 30,	
	2018	2017
Beginning balance as of December 31, 2017	\$ 146,496	\$ 156,206
Revenue recognized	1,774,620	1,667,090
Amounts collected or invoiced	(1,765,218)	(1,661,717)
Ending balance as of September 30, 2018	\$ 155,898	\$ 161,579

Note 9 – Inventories

Inventory costs are summarized as follows:

(in thousands)	September 30, 2018	December 31, 2017 (as adjusted)
Raw materials	\$ 311,190	\$ 258,228
Work in process	7,985	8,600
Finished goods	2,019	2,089

\$	321,194	\$	268,917
----	---------	----	---------

Note 10 – Accounts Receivable Sale Program

As of September 30, 2018, in connection with a trade accounts receivable sale program with an unaffiliated financial institution, the Company may elect to sell, at a discount, on an ongoing basis, up to a maximum of \$80.0 million of specific accounts receivable at any one time.

During each of the three months ended September 30, 2018 and 2017, the Company sold \$40.0 million of accounts receivable under this program, and in exchange, the Company received cash proceeds of \$39.9 million, net of the discount. During the nine months ended September 30, 2018 and 2017, the Company sold \$120.0 million and \$105.0 million, respectively, of accounts receivable under this program, and in exchange, the Company received cash proceeds of \$119.7 million and \$104.8 million, respectively, net of

the discount. The loss on the sale resulting from the discount was recorded to other expense within the Condensed Consolidated Statements of Income.

Note 11 – Income Taxes

Income tax expense consists of the following:

(in thousands)	Nine Months Ended September 30,	
	2018	2017 (as adjusted)
Federal – current	\$ 223	\$ (984)
Foreign – current	25,894	6,039
State – current	7,673	275
Deferred	11,863	581
	\$ 45,653	\$ 5,911

The U.S. Tax Cuts and Jobs Act (U.S. Tax Reform), which was signed into law on December 22, 2017, significantly changed U.S. tax law by, among other things, lowering corporate income tax rates, implementing a territorial tax system and imposing a transition tax on deemed repatriated earnings of foreign subsidiaries. The U.S. Tax Reform reduced the U.S. corporate income tax rate from a maximum of 35% to a flat 21% rate, effective January 1, 2018.

To minimize tax base erosion with a territorial tax system, the U.S. Tax Reform enacted a new global intangible low-taxed income (GILTI) provision. Under the GILTI provision, certain foreign subsidiary earnings in excess of an allowable return on the foreign subsidiary's depreciable tangible assets are included in U.S. taxable income offset by a limited deemed paid foreign tax credit. The Company is subject to the GILTI provisions due to its operations in foreign jurisdictions.

As of December 31, 2017, the Company had approximately \$928 million in cumulative undistributed foreign earnings outside the U.S. Substantially all of these undistributed earnings are subject to the U.S. mandatory repatriation tax and are eligible to be repatriated to the U.S. without additional U.S. tax under the U.S. Tax Reform. The Company has historically asserted its intention to indefinitely reinvest undistributed foreign earnings. The Company no longer considers these earnings to be indefinitely reinvested in its foreign subsidiaries. As a result of this change in assertion for undistributed earnings prior to December 31, 2017, the Company recorded \$30.7 million of deferred tax expense for foreign withholding tax from Asia and \$9.4 million of deferred U.S. state income tax expense in the first three months of 2018. During the nine months ended September 30, 2018, the Company repatriated \$522.0 million of foreign earnings to the U.S. For future undistributed earnings earned after December 31, 2017, the Company intends to indefinitely reinvest certain future undistributed foreign earnings from certain jurisdictions, and repatriate future earnings from other specific jurisdictions as part of its foreign cash management strategy around the world.

Excluding the impact of these items, income tax expense differs from the amount computed by applying the U.S. federal statutory income tax rate to income before income taxes primarily due to the mix of taxable income by taxing

jurisdiction, the impact of tax incentives and tax holidays in foreign locations, state income taxes (net of federal benefit) and the U.S. tax under GILTI.

The Company has been granted certain tax incentives, including tax holidays, for its subsidiaries in China, Malaysia and Thailand that will expire at various dates, unless extended or otherwise renegotiated, through 2018 in China, 2021 in Malaysia and 2028 in Thailand, and are subject to certain conditions with which the

Company expects to comply. The net impact of these tax incentives was to lower income tax expense for the nine months ended September 30, 2018 and 2017 by approximately \$8.2 million (approximately \$0.17 per diluted share) and \$7.3 million (approximately \$0.15 per diluted share), respectively, as follows:

(in thousands)	Nine Months Ended	
	September 30,	
	2018	2017
China	\$ 1,449	\$ 888
Malaysia	3,219	3,151
Thailand	3,579	3,294
	\$ 8,247	\$ 7,333

As of September 30, 2018, the total amount of the reserve for uncertain tax benefits including interest was \$0.3 million. The reserve is classified as a current or long-term liability in the condensed consolidated balance sheets based on the Company's expectation of when the items will be settled. The amount of accrued potential interest on unrecognized tax benefits included in the reserve as of September 30, 2018, was \$47.0 thousand. There was no reserve for potential penalties. During the nine months ended September 30, 2018, the Company released \$0.5 million of uncertain tax benefits from a U.S. Internal Revenue Service (IRS) audit related to the Secure Communication Systems, Inc. acquisition. During the first quarter of 2018, the IRS indicated that this examination of years 2013 to 2015 was closed. In addition, the IRS also notified the Company that the examination of the Company's consolidated U.S. income tax return filings for 2014 was also closed with no additional tax costs.

The Company and its subsidiaries in Brazil, China, Ireland, Luxembourg, Malaysia, Mexico, the Netherlands, Romania, Singapore, Thailand and the United States remain open to examination by the various local taxing authorities, in total or in part, for fiscal years 2011 to 2017. Currently, the Company does not have any ongoing income tax examinations by any jurisdiction. During the course of such income tax examinations, disputes may occur as to matters of fact or law. Also, in most tax jurisdictions, the passage of time without examination will result in the expiration of applicable statutes of limitations thereby precluding examination of the tax period(s) for which such statute of limitation has expired. The Company believes that it has adequately provided for its tax liabilities.

Note 12 – Segment and Geographic Information

The Company currently has manufacturing facilities in the Americas, Asia and Europe to serve its customers. The Company is operated and managed geographically, and management evaluates performance and allocates the Company's resources on a geographic basis. Intersegment sales are generally recorded at prices that approximate arm's length transactions. Operating segments' measure of profitability is based on income from operations. The accounting policies for the reportable operating segments are the same as for the Company taken as a whole. The Company has three reportable operating segments: Americas, Asia and Europe. Information about operating segments is as follows:

(in thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017 (as adjusted)	2018	2017 (as adjusted)
Net sales:				
Americas	\$ 404,137	\$ 379,417	\$ 1,217,200	\$ 1,146,171
Asia	210,153	208,207	602,903	581,991
Europe	43,054	43,826	140,205	127,480
Elimination of intersegment sales	(16,656)	(20,521)	(50,893)	(67,199)
	\$ 640,688	\$ 610,929	\$ 1,909,415	\$ 1,788,443
Depreciation and amortization:				
Americas	\$ 5,746	\$ 5,679	\$ 17,171	\$ 16,599
Asia	2,967	2,882	8,660	9,021
Europe	860	705	2,644	2,041
Corporate	4,987	3,008	11,168	8,930
	\$ 14,560	\$ 12,274	\$ 39,643	\$ 36,591
Income from operations:				
Americas	\$ 9,586	\$ 15,046	\$ 41,845	\$ 46,823
Asia	18,963	21,477	53,441	55,314
Europe	2,242	2,551	7,437	7,430
Corporate and intersegment eliminations	(19,834)	(18,171)	(59,450)	(54,651)
	\$ 10,957	\$ 20,903	\$ 43,273	\$ 54,916
Other income (expense):				
Interest expense	(3,822)	(2,324)	(8,543)	(6,861)
Interest income	1,619	1,334	5,197	3,621
Other expense	1,139	(394)	827	(1,305)
Income before income taxes	\$ 9,893	\$ 19,519	\$ 40,754	\$ 50,371
Capital expenditures:				
Americas	\$ 8,975	\$ 8,548	\$ 34,369	\$ 17,584
Asia	3,898	1,696	12,548	12,820
Europe	651	638	2,303	4,018
Corporate	1,046	475	3,713	3,314
	\$ 14,570	\$ 11,357	\$ 52,933	\$ 37,736

(in thousands)		September 30, 2018	December 31, 2017 (as adjusted)
Total assets:			
	Americas	\$ 848,998	\$ 812,187
	Asia	548,571	674,783
	Europe	144,352	470,786
	Corporate and other	398,850	151,548
		\$ 1,940,771	\$ 2,109,304

Geographic net sales information reflects the destination of the product shipped. Long-lived assets information is based upon the physical location of the asset.

(in thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017 (as adjusted)	2018	2017 (as adjusted)
Geographic net sales:				
	United States	\$ 438,461	\$ 403,233	\$ 1,280,026
	Asia	105,422	114,302	328,327
	Europe	69,289	71,718	222,870
	Other Foreign	27,516	21,676	78,192
		\$ 640,688	\$ 610,929	\$ 1,909,415
				\$ 1,788,443
Long-lived assets:			September 30, 2018	December 31, 2017
	United States		\$ 186,557	\$ 167,858
	Asia		79,351	77,750
	Europe		10,336	11,042
	Other		24,525	25,830
			\$ 300,769	\$ 282,480

Note 13 – Supplemental Cash Flow and Non-Cash Information

The following information concerns supplemental disclosures of cash payments.

(in thousands)	Three Months Ended September 30,		Nine Months Ended September 30,	
	2018	2017	2018	2017
Income taxes paid, net	\$ 15,544	\$ 2,524	\$ 39,296	\$ 5,049
Interest paid	1,845	2,089	6,163	6,385
Non-cash investing activity:				
Additions to property, plant and equipment in accounts payable			\$ 6,629	\$ 6,024

Note 14 – Contingencies

The Company is involved in various legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on the Company's consolidated financial position or results of operations.

Note 15 – Restructuring Charges

The Company has undertaken initiatives to restructure its business operations to improve utilization and realize cost savings. These initiatives have included changing the number and location of production facilities, largely to align 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 moving production between facilities, reducing staff levels, realigning our business processes, reorganizing our management and other activities.

The Company recognized restructuring charges during 2018 and 2017 primarily related to facility transition and closures in the Americas, capacity reduction and reductions in workforce in certain facilities across various regions. The following table summarizes the 2018 activity in the accrued restructuring balances related to the restructuring activities initiated prior to September 30, 2018:

(in thousands)	Balance as of December		Cash Payment	Non-Cash Activity	Foreign Exchange Adjustments	Balance as of September 30, 2018
	31, 2017	Restructuring Charges				
2018 Restructuring:						
Severance	\$ —	\$ 1,626	\$ (1,626)	\$ —	\$ —	—
Other exit costs	—	1,323	(687)	—	—	636
	—	2,949	(2,313)	—	—	636

Edgar Filing: BENCHMARK ELECTRONICS INC - Form 10-Q

2017 Restructuring:							
Severance	47	3	(50)	—	—	—	—
Leased facilities and equipment	—	96	(96)	—	—	—	—
Other exit costs	198	270	(309)	—	(29)	130	130
	245	369	(455)	—	(29)	130	130
2016 Restructuring:							
Severance	29	(6)	(23)	—	—	—	—
Other exit costs	16	245	(145)	(116)	—	—	—
	45	239	(168)	(116)	—	—	—
Total	\$ 290	\$ 3,557	\$ (2,936)	\$ (116)	\$ (29)	\$ 766	\$ 766

Note 16 – Fair Value

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. A three-tier fair value hierarchy of inputs is employed to determine fair value measurements.

- Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets and liabilities.
- Level 2 inputs are observable prices that are not quoted on active exchanges, such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.
- Level 3 inputs are unobservable inputs employed for measuring the fair value of assets or liabilities.

This hierarchy requires the Company to use observable market data, when available, and to minimize the use of unobservable inputs when determining fair value.

The Company's financial instruments include cash equivalents, accounts and other receivables, accounts payable, accrued liabilities and long-term debt and capital lease obligations. The Company believes that the carrying values of these instruments approximate fair value. As of September 30, 2018, the Company's long-term investments and derivative instruments were recorded at fair value using Level 3 inputs. The Company uses derivative instruments to manage the variability of foreign currency obligations and interest rates. The Company does not enter into derivatives for speculative purposes.

The forward currency exchange contracts in place as of September 30, 2018 have not been designated as accounting hedges and, therefore, changes in fair value are recorded within the Condensed Consolidated Statements of Income.

The Company has an interest rate swap agreement, with notional amounts of \$145.5 million and \$155.3 million as of September 30, 2018 and December 31, 2017, respectively, to hedge a portion of its interest rate exposure on outstanding borrowings under the Credit Agreement. Under this interest rate swap agreement, the Company receives variable rate interest payments based on the one-month LIBOR rate and pays fixed rate interest payments. The fixed interest rate for the contract is 1.4935%. The effect of this swap is to convert a portion of the floating rate interest expense to fixed interest rate expense. Based on the terms of the interest rate swap contract and the underlying borrowings outstanding under the Credit Agreement, the interest rate contract was determined to be effective, and thus qualifies and has been designated as a cash flow hedge. As such, changes in the fair value of the interest rate swap are recorded in other comprehensive income on the accompanying Condensed Consolidated Balance Sheets until earnings are affected by the variability of cash flows. The fair value of the interest rate swap was a \$3.5 million asset as of September 30, 2018 and a \$2.0 million asset as of December 31, 2017. During the nine months ended September 30, 2018, the Company recorded unrealized gain of \$1.5 million (\$1.2 million net of tax) on the swap in other comprehensive income. See Note 17.

Note 17 – Accumulated Other Comprehensive Loss

The changes in accumulated other comprehensive loss by component were as follows:

(in thousands)	Foreign currency translation adjustments	Derivative instruments, net of tax	Unrealized loss on investments, net of tax	Other	Total
Balances, December 31, 2017	\$ (9,567)	\$ 1,478	\$ (41)	\$ (19)	\$ (8,149)
Other comprehensive gain (loss) before reclassifications	(1,569)	1,159	41	—	(369)
Net current period other comprehensive gain (loss)	(1,569)	1,159	41	—	(369)
Balances, September 30, 2018	\$ (11,136)	\$ 2,637	\$ —	\$ (19)	\$ (8,518)

See Note 16 for further explanation of the change in derivative instruments that is recorded to Accumulated Other Comprehensive Loss.

Note 18 – Shareholders' EquityDividends

The Company began declaring and paying quarterly dividends during the first quarter of 2018. For the nine months ended September 30, 2018, cash dividends paid totaled \$14.2 million. On September 17, 2018, the Company declared a quarterly cash dividend of \$0.15 per share of the Company's common stock to shareholders of record as of September 28, 2018. The dividend of \$6.8 million was paid on October 11, 2018. The Board of Directors currently intends to continue paying quarterly dividends. However, the Company's future dividend policy is subject to the Company's compliance with applicable law, and depending on, among other things, the Company's results of operations, financial condition, level of indebtedness, capital requirements, contractual restrictions, restrictions in the Company's debt agreements, and other factors that the Board of Directors may deem relevant. Dividend payments are not mandatory or guaranteed; there can be no assurance that the Company will continue to pay a dividend in the future.

Share Repurchase Authorization

On March 6, 2018, the Board of Directors approved an expanded stock repurchase authorization granting the Company authority to repurchase up to \$250 million in common stock in addition to the \$100 million previously approved on December 7, 2015. As of September 30, 2018, the Company had \$191.4 million remaining under the stock repurchase authorization. On October 26, 2018, the Board of Directors authorized the repurchase of an additional \$100 million of the Company's common stock.

During the first quarter of 2018, the Company entered into an accelerated stock repurchase agreement (ASR) with a third party to repurchase an aggregate of \$50.0 million of the Company's common stock and received an initial delivery of 1.3 million shares of common stock. On July 18, 2018, the Company completed the ASR program and received delivery of the remaining shares totaling 0.4 million shares.

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

This quarterly report (this Report) contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended and Section 21E of the Securities Exchange Act of 1934, as amended (Exchange Act). These forward-looking statements are identified as any statement that does not relate strictly to historical or current facts and may include words such as "anticipate," "believe," "intend," "plan," "projection," "forecast," "strategy," "position," "continue," "estimate," "expect," "may," "will," or the negative or other variations thereof. In particular, statements, express or implied,

concerning future operating results or the ability to generate sales, income or cash flow are forward-looking statements. Undue reliance should not be placed on any forward-looking statements. Forward-looking statements are not guarantees of performance. They involve risks, uncertainties and assumptions that are beyond our ability to control or predict, including those discussed in Part I, Item 1A of the 2017 10-K and any added under Part II, Item 1A of this Report. Should one or more of these risks or uncertainties materialize, or should underlying assumptions prove incorrect, actual outcomes, including the future results of our operations, may vary materially from those indicated. The following discussion should be read in conjunction with the Condensed Consolidated Financial Statements and accompanying notes, and the 2017 10-K.

OVERVIEW

We are a worldwide provider of innovative product design, engineering services, technology solutions and advanced manufacturing services (both electronic manufacturing services (EMS) and precision technology manufacturing machining services). In this Report, references to Benchmark, the Company or use of the words “we”, “our” and “us” include Benchmark’s subsidiaries unless otherwise noted.

From initial product concept to volume production, including direct order fulfillment and aftermarket services, Benchmark has been providing integrated services and solutions to original equipment manufacturers since 1979. Today, Benchmark proudly serves the following industries: aerospace and defense, medical technologies, complex industrials, test and instrumentation, next-generation telecommunications and high-end computing.

Our customer engagement focuses on three principal areas:

- *Engineering Services*, which include design for manufacturability, manufacturing process and test development, concurrent and sustaining engineering, turnkey product design and regulatory services. Our engineering services may be for systems, sub-systems, printed circuit boards and assemblies, and components. We provide these services across all the industries we serve, but focus primarily in regulated industries such as medical, complex industrials, aerospace and defense, and next generation telecommunications.
- *Technology Solutions*, which involve developing a library of building blocks or reference designs primarily in defense solutions, surveillance systems, radio frequency and high-speed design, and front-end Internet-of-things data collection systems. We often merge these technology solutions with engineering services in support of manufacturing services. Our reference designs can be utilized across a variety of industries but we have significant capabilities for the aerospace and defense markets.
- *Manufacturing Services*, which include printed circuit board assemblies (PCBAs) and subsystem assembly, box build and systems integration. Systems integration is often building a finished assembly that includes PCBAs, complex

subsystem assemblies, mechatronics, displays, optics, and other components. These final products may be configured to order and delivered directly to the end-customer across all the industries we serve. Manufacturing services also includes precision technology manufacturing comprised of precision machining, advanced metal joining, assembly and functional testing primarily for customers in the test & instrumentation market (which includes semiconductor capital equipment) as well as the medical and aerospace and defense markets.

Our core strength lies in our ability to provide concept-to-production solutions in support of our customers. Our global manufacturing presence increases our ability to respond to our customers' needs by providing accelerated time-to-market and time-to-volume production of high-quality products – especially for complex products with lower volume and higher mix in regulated markets. These capabilities enable us to

build strong strategic relationships with our customers and to become an integral part of their business.

We believe our primary competitive advantages are our engineering services (including product design), technology solutions, and manufacturing services (including electronics and precision technology capabilities) provided by highly skilled personnel. We continue to invest in our business to expand our skills and service offerings from direct customer inputs. We have a closed-loop feedback system in place to respond to customer ideas to enhance our future flexible design and manufacturing solutions in support of the full life cycle of their products. These solutions provide accelerated time-to-market, faster time-to-volume production, and reduced product development costs. Working closely with our customers and responding promptly to their needs, we become an integral part of their process to bring products to market faster and more economically.

In addition, we believe that a strong focus on human capital through the talent we hire and retain is critical to maintaining our competitiveness. We are driving a customer-centric organization with a high degree of accountability and ownership to develop processes necessary to exceed customer expectations and deliver financial performance aligned to our goals. Through our employee feedback process, we solicit and act upon information to improve our company and better support our customers and business processes in the future. We have taken steps to attract the best leaders and are accelerating our efforts to mentor and develop key leaders for the future.

Our customers often face challenges in designing supply chains, planning demand, procuring materials and managing their inventories efficiently due to fluctuations in their customer demand, product design changes, short product life cycles and component price fluctuations.

We employ enterprise resource planning (ERP) systems and lean manufacturing principles to manage the procurement and manufacturing processes in an efficient and cost-effective manner so that, where possible, components arrive on a just-in-time, as-and-when-needed basis. Because we are a significant purchaser of electronic components and other raw materials, we are able to capitalize on the economies of scale associated with our relationships with suppliers to negotiate price discounts, obtain components and other raw materials that are in short supply, and return excess components. Our agility and expertise in supply chain management and our relationships with suppliers across the supply chain enable us to help reduce our customers' cost of goods sold and inventory exposure.

We recognize revenue from the sale of manufactured products built to customer specifications. We also generate revenue from design, development and engineering services, in addition to the sale of excess inventory.

Revenue is measured based on a consideration specified in a contract with a customer. We recognize revenue when we have satisfied a performance obligation by transferring control over a manufactured product to a customer. Our contracts with customers are generally short-term in nature. Customers are generally billed when the product is shipped or as services are performed. Under the majority of our manufacturing contracts with customers, the customer

controls all of the work-in-progress as products are being built. Revenues under these contracts are recognized progressively based on the cost-to-cost method. For other manufacturing contracts, the customer does not take control of the product until it is completed. Under these contracts, we recognize revenue upon transfer of control of product to the customer. Revenue from design, development and engineering services is recognized over time as the services are performed. We assume no significant obligations after shipment as we typically warrant workmanship only. Therefore, the warranty provisions are generally not significant.

Third Quarter 2018 Highlights

Sales for the three months ended September 30, 2018 increased 5% to \$640.7 million compared to \$610.9 million during the comparable 2017 period. During the third quarter of 2018, sales to customers in our various industry sectors fluctuated from the comparable 2017 period as follows:

- Industrials increased by 2%,
- A&D increased by 9%,
- Medical decreased by 6%,
- Test & Instrumentation decreased by 14%,
- Computing increased by 16%, and
- Telecommunications increased by 23%.

The overall revenue increase was driven primarily by demand increases in the Computing sector for enterprise storage products, in addition to increases in Telecommunication and A&D.

Our sales depend on the success of our customers, some of whom operate in businesses associated with rapid technological change and consequent product obsolescence. Developments adverse to our major customers or their products, or the failure of a major customer to pay for components or services, can adversely affect us. A substantial percentage of our sales is made to a small number of customers, and the loss of a major customer, if not replaced, would adversely affect us. Sales to our 10 largest customers represented 44% of our sales in both the nine months ended September 30, 2018 and 2017.

During the three months ended September 30, 2018, we incurred a \$3.4 million charge for the write-down of inventory and a provision to accounts receivable associated with the insolvency of a customer. These charges increased cost of sales by \$1.7 million and SG&A by \$1.7 million.

We experience fluctuations in gross profit from period to period. Different programs contribute different gross profits depending on factors such as the type of services involved, location of production, size of the program, complexity of the product and level of material costs associated with the various products. Moreover, new programs can contribute relatively less to our gross profit in their early stages when manufacturing volumes are usually lower, resulting in inefficiencies and unabsorbed manufacturing overhead costs. In addition, a number of our new and higher-volume programs remain subject to competitive constraints that can exert downward pressure on our margins. During periods of low production volume, we generally have idle capacity and reduced gross profit.

We have undertaken initiatives to restructure our business operations with the intention of improving utilization and reducing costs. During the first nine months of 2018, we recognized \$3.5 million of restructuring charges, primarily related to the closure of facilities in the Americas and reductions in workforce in certain facilities primarily in the Americas. In addition, we incurred \$2.3 million in costs related to the transition of our corporate headquarters to Arizona and \$2.0 million in costs associated with the write-off of existing deferred financing charges in connection with the refinancing of our credit facilities.

RESULTS OF OPERATIONS

The following table presents the percentage relationship that certain items in our Condensed Consolidated Statements of Income bear to sales for the periods indicated. The financial information and the discussion below should be read in conjunction with the Condensed Consolidated Financial Statements and Notes thereto in Part I, Item 1 of this Report.

	Three Months Ended		Nine Months Ended	
	September 30,	September 30,	September 30,	September 30,
	2018	2017	2018	2017
	(as adjusted)		(as adjusted)	
Sales	100.0%	100.0%	100.0%	100.0%
Cost of sales	91.8	90.5	91.3	90.8
Gross profit	8.2	9.5	8.7	9.2
Selling, general and administrative expenses	5.9	5.3	5.7	5.4
Amortization of intangible assets	0.4	0.4	0.4	0.4
Restructuring charges and other costs	0.3	0.4	0.3	0.3
Income from operations	1.7	3.4	2.3	3.1
Other expenses, net	(0.2)	(0.2)	(0.1)	(0.3)
Income before income taxes	1.5	3.2	2.1	2.8
Income tax expense	0.3	0.3	2.4	0.3
Net income (loss)	1.2%	2.9%	(0.3)%	2.5%

Sales

Sales for the third quarter of 2018 were \$640.7 million, a 5% increase from sales of \$610.9 million for the same quarter in 2017. Sales for the first nine months of 2018 were \$1.9 billion, a 7% increase from sales of \$1.8 billion for the same period in 2017. The following table sets forth, for the periods indicated, the percentages of our sales by industry sector.

	Three Months Ended		Nine Months Ended	
	September 30,	September 30,	September 30,	September 30,
	2018	2017	2018	2017
	(as adjusted)		(as adjusted)	
<u>Higher-Value Markets</u>				
Industrials	20%	21%	20%	21%
A&D	16	16	16	17
Medical	15	17	15	15
Test & Instrumentation	12	14	15	14
	63	68	66	67
<u>Traditional Markets</u>				
Computing	23	20	21	20
Telecommunications	14	12	13	13
	37	32	34	33
Total	100%	100%	100%	100%

Industrials. Third quarter sales increased 2% to \$128.3 million from \$125.9 million in 2017. Sales during the first nine months of 2018 increased 1% to \$372.0 million from \$367.9 million in the same period of 2017.

Aerospace and Defense. Third quarter sales increased 9% to \$105.0 million from \$96.3 million in 2017. Sales during the first nine months of 2018 were \$301.3 million compared to \$296.3 million in the same period of 2017. The increases were primarily due to greater demand for communication equipment and security products.

Medical. Third quarter sales decreased 6% to \$96.3 million from \$102.1 million in 2017 primarily from the timing of new program transitions. Sales increased 6% to \$290.1 million during the first nine months of 2018 from \$273.8 million in the same period of 2017 primarily due to increased demand and new programs.

Test & Instrumentation. Third quarter sales decreased 14% to \$76.6 million from \$89.1 million in 2017. Sales during the first nine months of 2018 increased 12% to \$285.3 million from \$253.7 million in the same period of 2017. The nine month increase is primarily due to the strong demand we saw in our precision manufacturing machining operations serving the semi-capital equipment market during the first half of 2018, partially offset by the slowdown experienced in the same market during the three months ended September 30, 2018.

Computing. Third quarter sales increased 16% to \$145.4 million from \$125.3 million in 2017, and increased 11% to \$409.6 million during the first nine months of 2018 from \$367.8 million in the same period of 2017. The increase is primarily due to strength in the demand from legacy storage products and data security customers.

Telecommunications. Third quarter sales increased 23% to \$89.1 million from \$72.2 million in 2018 and 2017, respectively, and increased 10% to \$251.1 million during the first nine months of 2018 from \$228.9 million in the same period of 2017 due to increased demand from existing customers and a ramp of a new satellite program.

Our international operations are subject to the risks of doing business abroad. See Part I, Item 1A of our 2017 10-K for factors pertaining to our international sales and fluctuations in the exchange rates of foreign currency and for further discussion of potential adverse effects in operating results associated with the risks of doing business abroad. During the first nine months of both 2018 and 2017, 46% and 47%, respectively of our sales were from our international operations.

Gross Profit

Gross profit decreased 9% to \$52.8 million for the three months ended September 30, 2018 from \$58.2 million in the same quarter of 2017, and was \$165.4 million for the nine months ended September 30, 2018 and \$165.3 million in

the same period of 2017. For the nine months ended September 30, 2018 and 2017, we incurred \$0.9 million and \$1.2 million, respectively, in net charges for the write-down of inventory associated with the insolvency of two customers. Including the initial inventory charges and the subsequent partial recoveries, gross margin was 8.2% and 8.7%, respectively, for the three and nine months ended September 30, 2018 and 9.5% and 9.2%, respectively, for the three and nine months ended September 30, 2017. Excluding these items, gross margin decreased to 8.5% and 8.7%, respectively, for the three and nine months ended September 30, 2018 from 9.3% and 9.3%, respectively, in the same periods of 2017 primarily due to an increase in lower-margin Computing sector sales, a decrease in higher-margin Test & Instrumentation sector sales and the impacts from Medical transitions, investments in engineering and solutions and new program ramp costs.

Selling, General and Administrative Expenses

SG&A increased by 17% to \$37.6 million in the third quarter of 2018 compared to \$32.1 million in 2017, and increased by 12% to \$109.2 million in the first nine months of 2018 compared to \$97.1 million in 2017. During both the third quarter of 2018 and the first quarter of 2017, we had \$1.7 million in charges for a provision to accounts receivable associated with the insolvency of two customers. Including this provision to accounts receivable, SG&A increased to 5.9% of sales for the third quarter of 2018 from 5.3% in 2017, and increased to 5.7% of sales for the first nine months of 2018 from 5.4% in 2017. Excluding this provision to accounts receivable, SG&A increased to 5.6% of sales for the third quarter of 2018 from 5.3% in 2017, and increased to 5.6% of sales for the first nine months of 2018 from 5.3% in 2017, primarily due to increased stock-based and variable compensation and the investment in our sales and marketing organization.

Restructuring Charges and Other Costs

During the first nine months of 2018, we recognized \$3.5 million of restructuring charges, primarily related to facility transitions in the Americas and reductions in workforce in certain facilities primarily in the Americas. In addition, during the first nine months of 2018 we incurred \$2.3 million in costs related to the transition of our corporate headquarters to Arizona. We expect to incur additional restructuring charges ranging from \$2.0 million to \$2.5 million in the fourth quarter of 2018. In the first nine months of 2017, we recognized \$4.0 million of restructuring charges, primarily related to reductions in workforce in certain facilities across various regions, and \$1.6 million in transition costs. See Note 15 to the Condensed Consolidated Financial Statements in Part I, Item 1 of this Report.

Interest Expense

Interest expense increased to \$8.5 million during the first nine months of 2018 from \$6.9 million during the comparable 2017 period due to the write-off of existing deferred financing charges in connection with the refinancing of our credit facilities offset by lower debt levels.

Interest Income

Interest income increased to \$5.2 million during the first nine months of 2018 from \$3.6 million during the comparable 2017 period due primarily to higher interest rates on invested cash equivalents.

Income Tax Expense

Income tax expense of \$45.7 million represented an effective tax rate of 112.0% for the first nine months of 2018, compared with \$5.9 million for the comparable 2017 period, which represented an effective tax rate of 11.7%. During the first quarter of 2018, we changed our historical repatriation strategy. We have historically asserted our intention to indefinitely reinvest undistributed foreign earnings. We no longer consider these earnings to be indefinitely reinvested in our foreign subsidiaries. As a result of this change in assertion for undistributed earnings prior to December 31, 2017, we recorded a \$30.7 million tax expense for foreign withholding tax from Asia and \$9.4 million for U.S. state income tax expense in the first quarter of 2018. In the second quarter of 2018 we recorded \$0.4 million of additional U.S. tax for the distributions from our foreign subsidiaries. In addition, during 2018 we released \$0.5 million of uncertain tax benefits from a U.S. Internal Revenue Service (IRS) audit related to the Secure Communication Systems, Inc. acquisition. During the first quarter of 2018, the IRS indicated that this examination of years 2013 to 2015 was closed. Excluding these tax items, the effective tax rate in the first nine months of 2018 would have been 13.7%.

We have been granted certain tax incentives, including tax holidays, for our subsidiaries in China, Malaysia and Thailand that will expire at various dates, unless extended or otherwise renegotiated, through 2018 in China, 2021 in Malaysia, and 2028 in Thailand. Our Chinese subsidiary is in the process of applying for a

new tax incentive for future years. See Note 11 to the Condensed Consolidated Financial Statements in Item 1 of this Report.

Net Income (Loss)

We reported a net loss of \$4.9 million, or \$0.10 per diluted share, for the first nine months of 2018, compared with net income of \$44.5 million, or \$0.88 per diluted share, for the same period in 2017. The net decrease of \$49.4 million from 2017 was primarily the result of the tax expense related to the change in our historical repatriation strategy discussed above.

LIQUIDITY AND CAPITAL RESOURCES

We have historically financed our organic growth and operations through funds generated from operations and occasional borrowings under our revolving credit facility. Cash and cash equivalents totaled \$475.7 million at September 30, 2018 and \$742.5 million at December 31, 2017, of which \$170.2 million and \$673.4 million, respectively, were held outside the U.S. in various foreign subsidiaries. During the nine months ended September 30, 2018, we repatriated \$522.0 million of foreign earnings to the U.S.

Cash used in operating activities during the first nine months was \$17.3 million for 2018 and consisted primarily of \$4.9 million of net loss adjusted for \$39.6 million of depreciation and amortization and \$11.9 million in deferred income taxes, a \$20.0 million increase in accounts receivable, a \$54.3 million increase in inventories and a \$12.6 million increase in accounts payable. The deferred income taxes are a result of the change in assertion related to undistributed foreign earnings. The increase in inventories is primarily related to raw materials in support of production. Working capital was \$1.0 billion at September 30, 2018 and \$1.2 billion at December 31, 2017.

We purchase components only after customer orders or forecasts are received, which mitigates, but does not eliminate, the risk of loss on inventories. Supplies of electronic components and other materials used in operations are subject to industry-wide shortages, which may increase the timing of when we can begin the manufacturing processes. In certain instances, suppliers may allocate available quantities to us. If shortages of these components and other material supplies used in operations occur, vendors may not ship the quantities we need for production, and we may be forced to delay shipments, which can increase backorders and impact cash flows.

Cash used in investing activities during the first nine months was \$55.0 million for 2018, primarily due to purchases of additional property, plant and equipment totaling \$50.4 million. The purchases of property, plant and equipment were primarily for machinery and equipment in the Americas and Asia.

Cash used in financing activities during the first nine months was \$193.7 million for 2018. Share repurchases totaled \$122.1 million, net principal payments on long-term debt totaled \$57.8 million, dividends totaled \$14.2 million, and we received \$3.5 million from the exercise of stock options.

Under the terms of our \$650.0 million Credit Agreement, in addition to the Term Loan facility, we have a \$500.0 million five-year revolving credit facility to be used for general corporate purposes, both with a maturity date of July 20, 2023. The Credit Agreement includes an accordion feature pursuant to which total commitments under the facility may be increased by an additional \$275.0 million, subject to satisfaction of certain conditions. As of September 30, 2018, we had \$150.0 million in borrowings outstanding under the Term Loan facility, \$2.8 million in letters of credit outstanding under the Revolving Credit Facility and \$497.2 million was available for future borrowing under the Revolving Credit Facility. See Note 7 to the Condensed Consolidated Financial Statements included in Part I, Item 1 of this Report for more information regarding the terms of the Credit Agreement.

The Credit Agreement contains certain financial covenants as to interest coverage and debt leverage, and certain customary affirmative and negative covenants, including restrictions on our ability to incur additional debt and liens, pay dividends, repurchase shares, sell assets and merge or consolidate with other persons. Amounts due under the Credit Agreement could be accelerated upon specified events of default, including a failure to pay amounts due, breach of a covenant, material inaccuracy of a representation, or occurrence of bankruptcy or insolvency, subject, in some cases, to cure periods. As of September 30, 2018, we were in compliance with all of these covenants and restrictions.

During the next 12 months, we believe our capital expenditures will approximate \$40 to \$50 million, principally for machinery and equipment as well as expansion investments to support our ongoing business around the globe.

Our operations, and the operations of businesses we acquire, are subject to certain foreign, federal, state and local regulatory requirements relating to environmental, waste management, health and safety matters. We believe we operate in substantial compliance with all applicable requirements and we seek to ensure that newly acquired businesses comply or will comply substantially with applicable requirements. To date, the costs of compliance and workplace and environmental remediation have not been material to us. However, material costs and liabilities may arise from these requirements or from new, modified or more stringent requirements in the future. In addition, our past, current and future operations, and the operations of businesses we have or may acquire, may give rise to claims of exposure by employees or the public, or to other claims or liabilities relating to environmental, waste management or health and safety concerns.

On March 6, 2018, our Board of Directors approved an expanded stock repurchase program granting us the authority to repurchase up to \$250 million in common stock in addition to the \$100.0 million approved on December 7, 2015. As of September 30, 2018, we had \$191.4 million remaining under the share repurchase authorization to purchase additional shares. On October 26, 2018, the Board of Directors authorized an additional \$100 million shares for repurchase above our existing program. As of November 7, 2018, we had \$253 million remaining under the share repurchase authorization. We are under no commitment or obligation to repurchase any particular amount of common stock.

Management believes that our existing cash balances and funds generated from operations will be sufficient to permit us to meet our liquidity requirements over the next 12 months. Management further believes that our ongoing cash flows from operations and any borrowings we may incur under our revolving credit facility will enable us to meet operating cash requirements in future years. If we consummated significant acquisitions in the future, our capital needs would increase and could possibly result in our need to increase available borrowings under our Credit Agreement or access public or private debt and equity markets. There can be no assurance, however, that we would be successful in raising additional debt or equity on acceptable terms.

CONTRACTUAL OBLIGATIONS

We have certain contractual obligations for operating and capital leases that were summarized in a table of Contractual Obligations in our 2017 10-K. There have been no material changes to our contractual obligations, outside of the ordinary course of our business, since December 31, 2017.

OFF-BALANCE SHEET ARRANGEMENTS

As of September 30, 2018, we did not have any significant off-balance sheet arrangements. See Note 16 to the Condensed Consolidated Financial Statements.

CRITICAL ACCOUNTING POLICIES AND ESTIMATES AND RECENTLY ENACTED ACCOUNTING PRINCIPLES

Management's discussion and analysis is based upon our condensed consolidated financial statements, which have been prepared in accordance with U.S. GAAP. Our significant accounting policies are summarized in Note 1 to the Consolidated Financial Statements included in our 2017 10-K. Also, see Note 2 to the Condensed Consolidated Financial Statements above for a discussion of recently enacted accounting principles.

Item 3 – Quantitative and Qualitative Disclosures About Market Risk

Our international sales comprise a significant portion of our net sales. We are exposed to risks associated with operating internationally, including:

- Foreign currency exchange risk;
- Import and export duties, taxes and regulatory changes;
- Inflationary economies or currencies; and
- Economic and political instability.

Additionally, some of our operations are in developing countries. Certain events, including natural disasters, can impact the infrastructure of a developing country more severely than they would impact the infrastructure of a developed country. A developing country can also take longer to recover from such events, which could lead to delays in our ability to resume full operations.

We transact business in various foreign countries and are subject to foreign currency fluctuation risks. We use natural hedging and forward contracts to economically hedge transactional exposure primarily associated with trade accounts receivable, other receivables and trade accounts payable that are denominated in a currency other than the functional currency of the respective operating entity. We do not use derivative financial instruments for speculative purposes. The forward contracts in place as of September 30, 2018 have not been designated as accounting hedges and, therefore, changes in fair value are recorded within our Consolidated Statements of Income.

Our sales are substantially denominated in U.S. dollars. Our foreign currency cash flows are generated in certain European and Asian countries and Mexico.

We are also exposed to market risk for changes in interest rates on our financial instruments, a portion of which relates to our invested cash balances. We do not use derivative financial instruments in our investing activities. We place cash and cash equivalents and investments with various major financial institutions. We protect our invested principal funds by limiting default risk, market risk and reinvestment risk. We mitigate default risk by generally investing in investment-grade securities.

We are also exposed to interest rate risk on borrowings under our Credit Agreement. As of September 30, 2018, we had \$150.0 million outstanding on the floating rate Term Loan facility, and we have an interest rate swap agreement with a notional amount of \$145.5 million. Under this swap agreement, we receive variable rate interest payments and pay fixed rate interest payments. The effect of this swap is to convert a portion of our floating rate interest expense to fixed interest rate expense. The interest rate swap is designated as a cash flow hedge. For additional information, see Note 16 to the Condensed Consolidated Financial Statements in Item 1 of this Report.

On October 26, 2018, the Company entered into a new swap agreement, which is effective October 31, 2018. Under the new swap agreement, the Company will receive variable rate payments based on the one-

month LIBOR rate and pay fixed rate interest payments. The fixed interest rate for the contract is 2.928%. Based on the terms of this agreement, the interest rate contract has been determined to be effective and has been designated a cash flow hedge. On October 30, 2018, the Company terminated its existing interest rate swap agreement and received \$3.5 million, which represented the fair value of the agreement as of the termination date. This gain, which is included in accumulated other comprehensive loss, will be amortized over the original term of the agreement through November 2020 using the interest rate method and will be recorded against interest expense.

Item 4 – Controls and Procedures

As of the end of the period covered by this Report, the Company's management (with the participation of our Chief Executive Officer (CEO) and Chief Financial Officer (CFO)) conducted an evaluation pursuant to Rule 13a-15 under the Exchange Act, of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in Rule 13a-15(e) or 15d-15(e) of the Exchange Act). Based on this evaluation, the CEO and CFO concluded that as of the end of the period covered by this Report such disclosure controls and procedures were effective to provide reasonable assurance that information required to be disclosed by the Company in reports it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the rules and forms of the SEC, and include controls and procedures designed to ensure that information required to be disclosed by the Company in such reports is accumulated and communicated to our management, including the CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

There has been no change in our internal control over financial reporting (as defined in Rule 13a-15(f) or 15d-15(f) of the Exchange Act) that occurred during the last fiscal quarter covered by this Report that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within a company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple errors or mistakes. Additionally, controls can be circumvented by individuals' acts, by collusion of two or more people, or by management overriding the control. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, a control may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate.

PART II—OTHER INFORMATION**Item 1. Legal Proceedings**

We are involved in various legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on our consolidated financial position or results of operations.

Item 1A. Risk Factors

There are no material changes to the risk factors set forth in Part I, Item 1A of our 2017 10-K.

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

(c) The following table provides information for the quarter ended September 30, 2018 about the Company's repurchases of its equity securities registered pursuant to Section 12 of the Exchange Act, at a total cost of \$46.2 million:

ISSUER PURCHASES OF EQUITY SECURITIES

Period	(a) Total Number of Shares (or Units) Purchased⁽¹⁾	(b) Average Price Paid per Share (or Unit)⁽²⁾	(c) Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs	(d) Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs⁽³⁾
July 1 to 31, 2018	601,997	\$24.43	601,997	\$232.8 million
August 1 to 31, 2018	915,378	\$25.55	915,378	\$209.4 million
September 1 to 30, 2018	708,833	\$25.47	708,833	\$191.4 million
Total	2,226,208	\$25.22	2,226,208	

⁽¹⁾ All stock repurchases were made on the open market.

⁽²⁾ Average price paid per share is calculated on a settlement basis and excludes commission.

⁽³⁾ On March 6, 2018, the Board of Directors approved an expanded stock repurchase authorization granting the Company authority to repurchase up to \$250 million in common stock in addition to the \$100 million previously

approved on December 7, 2015. As of September 30, 2018, the Company had \$191.4 million remaining under the stock repurchase authorization. On October 26, 2018, the Board of Directors authorized the repurchase of an additional \$100 million of the Company's common stock. Net of shares repurchased to date, the total remaining authorization outstanding as of November 7, 2018 is \$253 million. Stock purchases may be made in the open market, in privately negotiated transactions or block transactions, at the discretion of the Company's management and as market conditions warrant. Purchases are funded from available cash and may be commenced, suspended or discontinued at any time without prior notice. Shares of stock repurchased under the program are retired.

During the first quarter of 2018, the Company entered into an accelerated stock repurchase agreement (ASR) with a third party to purchase shares of its common stock for a payment of \$50.0 million and received an initial delivery of 1.3 million shares of common stock. See Note 18 to the Condensed Consolidated Financial Statements in Item 1 of this report. On July 18, 2018, the Company completed the ASR program and received delivery of the remaining shares totaling 0.4 million shares.

Item 6. Exhibits

Exhibit Number	Description of Exhibit
3.1	<u>Restated Certificate of Formation dated May 17, 2016 (incorporated by reference to Exhibit 3.1 to the Company's Current Report on Form 8-K dated May 17, 2016) (the 8-K) (Commission file number 1-10560)</u>
3.2	<u>Amended and Restated Bylaws of the Company dated May 11, 2016 (incorporated by reference to Exhibit 3.2 to the 8-K)</u>
4.1	<u>Specimen form of certificate evidencing the Common Shares (incorporated by reference to Exhibit 4.1 to the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2014) (Commission file number 1-10560)</u>
31.1 ⁽¹⁾	<u>Section 302 Certification of Chief Executive Officer</u>
31.2 ⁽¹⁾	<u>Section 302 Certification of Chief Financial Officer</u>
32.1 ⁽¹⁾	<u>Section 1350 Certification of Chief Executive Officer</u>
32.2 ⁽¹⁾	<u>Section 1350 Certification of Chief Financial Officer</u>
101.INS ⁽²⁾	XBRL Instance Document
101.SCH ⁽²⁾	XBRL Taxonomy Extension Schema Document
101.CAL ⁽²⁾	XBRL Taxonomy Extension Calculation Linkbase Document

101.LAB ⁽²⁾ XBRL Taxonomy Extension Label Linkbase Document

101.PRE ⁽²⁾ XBRL Taxonomy Extension Presentation Linkbase Document

101.DEF ⁽²⁾ XBRL Taxonomy Extension Definition Linkbase Document

⁽¹⁾ Filed herewith.

⁽²⁾ XBRL (Extensible Business Reporting Language) information is furnished and not filed or a part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, is deemed not filed for purposes of Section 18 of the Securities Exchange Act of 1934 and otherwise is not subject to liability under these sections.

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 on November 8, 2018.

	BENCHMARK ELECTRONICS, INC.
	(Registrant)
	By: <u>/s/ Paul J. Tufano</u>
	Paul J. Tufano
	President and Chief Executive Officer
	(Principal Executive Officer)
	By: <u>/s/ Roop K. Lakkaraju</u>
	Roop K. Lakkaraju
	Chief Financial Officer
	(Principal Financial Officer)