

PLEXUS CORP
Form 10-Q
February 04, 2011

Table of Contents

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q**

(X) Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
For the quarterly period ended January 1, 2011
or

() Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
Commission File Number 001-14423

PLEXUS CORP.

(Exact name of registrant as specified in charter)

Wisconsin 39-1344447
(State of Incorporation) (IRS Employer
Identification No.)

One Plexus Way

Neenah, Wisconsin 54956

(Address of principal executive offices)(Zip Code)

Telephone Number (920) 722-3451

(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 a No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes a No

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

Large accelerated filer a Accelerated filer

Non-accelerated filer Smaller reporting company

(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No a

As of January 31, 2011, there were 40,535,848 shares of Common Stock of the Company outstanding.

PLEXUS CORP.
TABLE OF CONTENTS
January 1, 2011

<u>PART I. FINANCIAL INFORMATION</u>	3
<u>ITEM 1. FINANCIAL STATEMENTS</u>	3
<u>Condensed Consolidated Statements of Operations and Comprehensive Income</u>	3
<u>Condensed Consolidated Balance Sheets</u>	4
<u>Condensed Consolidated Statements of Cash Flows</u>	5
<u>Notes to Condensed Consolidated Financial Statements</u>	6
<u>ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS</u>	17
<u>Safe Harbor Cautionary Statement</u>	17
<u>Overview</u>	18
<u>Executive Summary</u>	19
<u>Results of Operations</u>	20
<u>Liquidity and Capital Resources</u>	22
<u>Reportable Segments</u>	24
<u>Contractual Obligations, Commitments and Off-Balance Sheet Obligations</u>	25
<u>Disclosure About Critical Accounting Policies</u>	26
<u>New Accounting Pronouncements</u>	26
<u>ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	26
<u>ITEM 4. CONTROLS AND PROCEDURES</u>	27
<u>PART II. OTHER INFORMATION</u>	28
<u>ITEM 1. Legal Proceedings</u>	28
<u>ITEM 1A. Risk Factors</u>	28
<u>ITEM 6. Exhibits</u>	28

SIGNATURES

30

EX-31.1

EX-31.2

EX-32.1

EX-32.2

EX-101 INSTANCE DOCUMENT

EX-101 SCHEMA DOCUMENT

EX-101 CALCULATION LINKBASE DOCUMENT

EX-101 LABELS LINKBASE DOCUMENT

EX-101 PRESENTATION LINKBASE DOCUMENT

2

Table of Contents**PART I. FINANCIAL INFORMATION****ITEM 1. FINANCIAL STATEMENTS**

PLEXUS CORP. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
AND COMPREHENSIVE INCOME

(in thousands, except per share data)

Unaudited

	Three Months Ended	
	January 1, 2011	January 2, 2010
Net sales	\$565,774	\$430,399
Cost of sales	510,864	385,858
Gross profit	54,910	44,541
Selling and administrative expenses	27,061	24,319
Operating income	27,849	20,222
Other income (expense):		
Interest expense	(2,181)	(2,559)
Interest income	293	456
Miscellaneous	(141)	(95)
Income before income taxes	25,820	18,024
Income tax expense	787	180
Net income	\$ 25,033	\$ 17,844
Earnings per share:		
Basic	\$ 0.62	\$ 0.45
Diluted	\$ 0.61	\$ 0.44
Weighted average shares outstanding:		
Basic	40,468	39,587
Diluted	41,210	40,252
Comprehensive income:		

Edgar Filing: PLEXUS CORP - Form 10-Q

Net income	\$ 25,033	\$ 17,844
Derivative instrument fair market value adjustment net of income tax	188	699
Foreign currency translation adjustments	818	(255)
Comprehensive income	\$ 26,039	\$ 18,288

See notes to condensed consolidated financial statements.

3

Table of Contents**PLEXUS CORP. AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS**

(in thousands, except per share data)

Unaudited

	January 1, 2011	October 2, 2010
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 149,498	\$ 188,244
Accounts receivable, net of allowances of \$1,700 and \$1,400, respectively	318,533	311,205
Inventories	521,391	492,430
Deferred income taxes	21,363	18,959
Prepaid expenses and other	16,872	15,153
Total current assets	1,027,657	1,025,991
Property, plant and equipment, net	235,568	235,714
Deferred income taxes	9,620	11,787
Other	17,263	16,887
Total assets	\$1,290,108	\$1,290,379
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Current portion of long-term debt and capital lease obligations	\$ 17,052	\$ 17,409
Accounts payable	346,622	360,686
Customer deposits	29,581	27,301
Accrued liabilities:		
Salaries and wages	32,105	46,639
Other	53,080	50,484
Total current liabilities	478,440	502,519
Long-term debt and capital lease obligations, net of current portion	108,220	112,466
Other liabilities	22,974	23,539
Total non-current liabilities	131,194	136,005
Commitments and contingencies (Note 12)	-	-

Edgar Filing: PLEXUS CORP - Form 10-Q

Shareholders' equity:

Preferred stock, \$.01 par value, 5,000 shares authorized, none issued or outstanding	-	-
Common stock, \$.01 par value, 200,000 shares authorized, 47,957 and 47,849 shares issued, respectively, and 40,511 and 40,403 shares outstanding, respectively	480	478
Additional paid-in capital	401,632	399,054
Common stock held in treasury, at cost, 7,446 shares for both periods	(200,110)	(200,110)
Retained earnings	470,601	445,568
Accumulated other comprehensive income	7,871	6,865
Total shareholders' equity	680,474	651,855
Total liabilities and shareholders' equity	\$1,290,108	\$1,290,379

See notes to condensed consolidated financial statements.

Table of Contents**PLEXUS CORP. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(in thousands)

Unaudited

	Three Months Ended	
	January 1, 2011	January 2, 2010
Cash flows from operating activities		
Net income	\$ 25,033	\$ 17,844
Adjustments to reconcile net income to cash flows from operating activities:		
Depreciation	11,305	9,054
Gain on sale of property, plant and equipment	(16)	(5)
Deferred income taxes	(262)	(1,029)
Stock based compensation expense	2,388	1,839
Changes in operating assets and liabilities:		
Accounts receivable	(6,947)	(40,531)
Inventories	(28,558)	(50,253)
Prepaid expenses and other	(2,101)	(1,507)
Accounts payable	(12,611)	52,160
Customer deposits	2,276	(2,374)
Accrued liabilities and other	(11,635)	4,537
Cash flows used in operating activities	(21,128)	(10,265)
Cash flows from investing activities		
Payments for property, plant and equipment	(13,263)	(12,315)
Proceeds from sales of property, plant and equipment	43	11
Cash flows used in investing activities	(13,220)	(12,304)
Cash flows from financing activities		
Payments on debt and capital lease obligations	(4,663)	(4,194)
Proceeds from exercise of stock options	60	1,870
Income tax benefit of stock option exercises	132	175
Cash flows used in financing activities	(4,471)	(2,149)
Effect of exchange rate changes on cash and cash Equivalents	73	267

Edgar Filing: PLEXUS CORP - Form 10-Q

Net decrease in cash and cash equivalents	(38,746)	(24,451)
Cash and cash equivalents:		
Beginning of period	188,244	258,382
End of period	\$ 149,498	\$ 233,931

See notes to condensed consolidated financial statements.

5

Table of Contents

PLEXUS CORP. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
FOR THE THREE MONTHS ENDED JANUARY 1, 2011 AND JANUARY 2, 2010

Unaudited

NOTE 1 - BASIS OF PRESENTATION AND ACCOUNTING POLICIES

Basis of Presentation

The accompanying condensed consolidated financial statements included herein have been prepared by Plexus Corp. and its subsidiaries (Plexus or the Company) without audit and pursuant to the rules and regulations of the United States Securities and Exchange Commission (SEC). In the opinion of the Company, the accompanying condensed consolidated financial statements reflect all adjustments, which include normal recurring adjustments necessary for the fair statement of the consolidated financial position of the Company as of January 1, 2011, and the results of operations for the three months ended January 1, 2011 and January 2, 2010, and the cash flows for the same three month periods.

Certain information and footnote disclosures, normally included in financial statements prepared in accordance with generally accepted accounting principles, have been condensed or omitted pursuant to the SEC rules and regulations dealing with interim financial statements. However, the Company believes that the disclosures made in the condensed consolidated financial statements included herein are adequate to make the information presented not misleading. It is suggested that these condensed consolidated financial statements be read in conjunction with the consolidated financial statements and notes thereto included in the Company s 2010 Annual Report on Form 10-K.

The Company s fiscal year ends on the Saturday closest to September 30. The Company also uses a 4-4-5 weekly accounting system for the interim periods in each quarter. Each quarter therefore ends on a Saturday at the end of the 4-4-5 period. Periodically, an additional week must be added to the fiscal year to re-align with the Saturday closest to September 30. The accounting periods for the three months ended January 1, 2011 and January 2, 2010 each included 91 days.

In the fiscal first quarter of 2011, we completed our migration to a regional reporting structure. This change included establishing regional targets for various financial metrics, delegating additional authority to the regions to manage their business, and changing our related internal reporting. Given this change to regional reporting and management as well as in the information used by management for assessing performance and allocating Company resources, we modified our reporting segments. Prior to fiscal 2011, the Company s reportable segments consisted of the United States, Asia, Europe and Mexico. We have combined our United States and Mexico segments into the Americas (AMER) segment and renamed our Asia segment Asia Pacific (APAC) and our Europe segment Europe, Middle East and Africa (EMEA) to better represent our long-range regional focus. As a result, we have conformed all prior period segment presentations to be consistent with our current reportable segments. See Note 9 in Notes to Condensed Consolidated Financial Statements for further information.

Cash and Cash Equivalents:

Cash and cash equivalents include highly liquid investments with original maturities of three months or less at the time of purchase.

Fair Value of Financial Instruments

The Company holds financial instruments consisting of cash and cash equivalents, accounts receivable, accounts payable, debt, and capital lease obligations. The carrying value of cash and cash equivalents, accounts receivable, accounts payable and capital lease obligations as reported in the condensed consolidated financial statements approximates fair value. Accounts receivable were reflected at net realizable value based on anticipated losses due to potentially uncollectible balances. Anticipated losses were based on management s analysis of historical losses and changes in customers credit status. The fair value of the Company s term loan debt was \$101.6 million and \$105.2 million as of January 1, 2011 and October 2, 2010, respectively. The carrying value of the Company s term loan debt was \$108.8 million and \$112.5 million as of January 1, 2011 and October 2, 2010,

Table of Contents

respectively. The Company uses quoted market prices when available or discounted cash flows to calculate the fair value of its term loan debt.

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (or 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. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs. The accounting guidance establishes a fair value hierarchy based on three levels of inputs that may be used to measure fair value. The input levels are:

Level 1: Quoted (observable) market prices in active markets for identical assets or liabilities.

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

Level 3: Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the asset or liability.

NOTE 2 - INVENTORIES

Inventories are stated at the lower of cost (on a first-in, first-out basis) or market value. The stated cost is comprised of direct materials, labor, and overhead. The major classes of inventories, net of applicable lower of cost or market write-downs, were as follows (in thousands):

	January 1, 2011	October 2, 2010
Raw materials	\$389,109	\$365,883
Work-in-process	52,830	56,036
Finished goods	79,452	70,511
	\$521,391	\$492,430

Per contractual terms, customer deposits are received by the Company to offset obsolete and excess inventory risks. The total amount of customer deposits related to inventory and included within current liabilities on the accompanying Condensed Consolidated Balance Sheets as of January 1, 2011 and October 2, 2010 was \$28.2 million and \$25.8 million, respectively.

NOTE 3 - PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consisted of the following categories (in thousands):

	January 1, 2011	October 2, 2010
Land, buildings and improvements	\$ 148,175	\$ 138,230
Machinery and equipment	261,997	255,138
Computer hardware and software	80,958	79,108
Construction in progress	13,210	22,145
	504,340	494,621
Less: accumulated depreciation	(268,772)	(258,907)
	\$ 235,568	\$ 235,714

NOTE 4 - LONG-TERM DEBT

On April 4, 2008, the Company entered into its credit agreement (the Credit Facility) with a group of banks which allows the Company to borrow \$150 million in term loans and \$100 million in revolving loans. The \$150 million in term loans was immediately funded and the \$100 million revolving credit facility is currently

Table of Contents

available. The Credit Facility is unsecured and the revolving credit facility may be increased by an additional \$100 million (the accordion feature) if the Company has not previously terminated all or any portion of the Credit Facility, there is no event of default existing under the Credit Facility and both the Company and the administrative agent consent to the increase. The Credit Facility expires on April 4, 2013. Borrowings under the Credit Facility may be either through term loans or revolving or swing loans or letter of credit obligations. As of January 1, 2011, the Company has term loan borrowings of \$108.8 million outstanding and no revolving borrowings under the Credit Facility.

The Credit Facility contains certain financial covenants, which include a maximum total leverage ratio, maximum value of fixed rentals and operating lease obligations, a minimum interest coverage ratio and a minimum net worth test, all as defined in the agreement. As of January 1, 2011, the Company was in compliance with all debt covenants. If the Company incurs an event of default, as defined in the Credit Facility (including any failure to comply with a financial covenant), the group of banks has the right to terminate the remaining Credit Facility and all other obligations, and demand immediate repayment of all outstanding sums (principal and accrued interest). The interest rate on the borrowing varies depending upon the Company's then-current total leverage ratio; as of January 1, 2011, the Company could elect to pay interest at a defined base rate or the LIBOR rate plus 1.00%. Rates would increase upon negative changes in specified Company financial metrics and would decrease upon reduction in the current total leverage ratio to no less than LIBOR plus 1.00%. The Company is also required to pay an annual commitment fee on the unused credit commitment based on its leverage ratio; the current fee is 0.25%. Unless the accordion feature is exercised, this fee applies only to the initial \$100 million of availability (excluding the \$150 million of term borrowings). Origination fees and expenses associated with the Credit Facility totaled approximately \$1.3 million and have been deferred. These origination fees and expenses are being amortized over the five-year term of the Credit Facility. Equal quarterly principal repayments of the term loan of \$3.75 million per quarter began on June 30, 2008 and end on April 4, 2013, with a balloon repayment of \$75.0 million.

The Credit Facility allows for the future payment of cash dividends or the future repurchases of shares provided that no event of default (including any failure to comply with a financial covenant) is existing at the time of, or would be caused by, a dividend payment or a share repurchase.

Interest expense related to the commitment fee and amortization of deferred origination fees and expenses for the Credit Facility totaled approximately \$0.2 million for both the three months ended January 1, 2011 and January 2, 2010.

NOTE 5 - DERIVATIVES AND FAIR VALUE MEASUREMENTS

All derivatives are recognized in the accompanying Condensed Consolidated Balance Sheets at their estimated fair value. On the date a derivative contract is entered into, the Company designates the derivative as a hedge of a recognized asset or liability (a fair value hedge), a hedge of a forecasted transaction or of the variability of cash flows to be received or paid related to a recognized asset or liability (a cash flow hedge), or a hedge of the net investment in a foreign operation. The Company currently has cash flow hedges related to variable rate debt and foreign currency obligations. The Company does not enter into derivatives for speculative purposes. Changes in the fair value of the derivatives that qualify as cash flow hedges are recorded in Accumulated other comprehensive income in the accompanying Condensed Consolidated Balance Sheets until earnings are affected by the variability of the cash flows.

In June 2008, the Company entered into three interest rate swap contracts related to the \$150 million in term loans under the Credit Facility that had an initial total notional value of \$150 million and mature on April 4, 2013. These interest rate swap contracts will pay the Company variable interest at the three month LIBOR rate, and the Company will pay the counterparties a fixed interest rate. The fixed interest rates for each of these contracts are 4.415%, 4.490% and 4.435%, respectively. These interest rate swap contracts were entered into to convert \$150 million of the variable rate term loan under the Credit Facility into fixed rate debt. Based on the terms of the interest rate swap contracts and the underlying debt, these interest rate contracts were determined to be effective, and thus qualify as a cash flow hedge. As such, any changes in the fair value of these interest rate swaps are recorded in Accumulated other comprehensive income on the accompanying Condensed Consolidated Balance Sheets until earnings are affected by the variability of cash flows. The total fair value of these interest rate swap contracts was

\$7.7 million as of January 1, 2011. As of January 1, 2011, the total combined notional amount of the Company's three interest rate swaps was \$108.8 million.

Table of Contents

The Company's Malaysian operations have entered into forward exchange contracts on a rolling basis with a total notional value of \$41.0 million as of January 1, 2011. These forward contracts will fix the exchange rates on foreign currency cash used to pay a portion of local currency expenses. The changes in the fair value of the forward contracts are recorded in Accumulated other comprehensive income on the accompanying Condensed Consolidated Balance Sheets until earnings are affected by the variability of cash flows. The total fair value of the forward contracts was \$2.0 million as of January 1, 2011.

Table of Contents

The tables below present information regarding the fair values of derivative instruments (as defined in Note 1 in Condensed Consolidated Financial Statements - Fair Value of Financial Instruments) and the effects of derivative instruments on the Company's Condensed Consolidated Statements of Operations:

Fair Values of Derivative Instruments

In thousands of dollars

	Asset Derivatives		Liability Derivatives	
	January 1, 2011	October 2, 2010	January 1, 2011	October 2, 2010
Derivatives designated as hedging instrument	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Interest rate swaps	-	-	Current liabilities	
			Other	\$3,410
Interest rate swaps	-	-	Other liabilities	\$5,423
Forward contracts and other	Prepaid expenses and other \$1,963	\$2,612		-

The Effect of Derivative Instruments on the Condensed Consolidated Statements of Operations for the Three Months Ended

In thousands of dollars

	Amount of Gain or (Loss) Recognized in	Location of Gain	Amount of Gain or (Loss)	Location of Gain or (Loss)	Derivative (Ineffective) Portion and Amount	Derivative (Effective) Portion and Amount
Derivatives in Cash	on	from	Reclassified from	Amount	Amount	Amount

Edgar Filing: PLEXUS CORP - Form 10-Q

	Derivative (Effective Portion)		Accumulated OCI into Income (Effective Portion)		Excluded OCI from Testing		Excluded OCI from Testing	
Flow Hedging Relationships	January 1, 2011	January 2, 2010	January 1, 2011	January 2, 2010	January 1, 2011	January 2, 2010	January 1, 2011	January 2, 2010
Interest rate swaps	\$ 242	\$ 47	Interest income (expense) Selling and administrative expenses	\$(1,124)	\$(1,296)	Other income (expense)	\$-	\$-
Forward contracts	\$ 362	\$ 316	Interest income (expense) Selling and administrative expenses	\$11	\$ 157	Other income (expense)	\$-	\$-

Table of Contents

The following table lists the fair values of the Company's derivatives as of January 1, 2011, by input level as defined above:

	Fair Value Measurements Using Input Levels:			
	(in thousands)			
	Level 1	Level 2	Level 3	Total
Derivatives				
Interest rate swaps	\$ -	\$ 7,673	\$ -	\$ 7,673
Foreign currency forward contracts	\$ -	\$ 1,963	\$ -	\$ 1,963

The fair value of interest rate swaps and foreign currency forward contracts is determined using a market approach which includes obtaining directly or indirectly observable values from third parties active in the relevant markets. The primary input in the fair value of the interest rate swaps is the relevant LIBOR forward curve. Inputs in the fair value of the foreign currency forward contracts include prevailing forward and spot prices for currency and interest rate forward curves.

As of January 1, 2011, we held \$2.0 million of auction rate securities maturing on March 17, 2042, which were classified as other long-term assets and whose underlying assets are in guaranteed student loans that are backed by a U.S. government agency. If the credit quality deteriorates for these adjustable rate securities, we may in the future be required to record an impairment charge on these investments. The fair value of the auction rate securities approximates the carrying value of \$2.0 million as of January 1, 2011. We believe that these securities are marketable.

NOTE 6 - EARNINGS PER SHARE

The following is a reconciliation of the amounts utilized in the computation of basic and diluted earnings per share (in thousands, except per share amounts):

	Three Months Ended	
	January 1, 2011	January 2, 2010
<u>Basic and Diluted Earnings Per Share:</u>		
Net income	\$25,033	\$17,844
Basic weighted average common shares outstanding	40,468	39,587
Dilutive effect of stock options	742	665
Diluted weighted average shares outstanding	41,210	40,252

Edgar Filing: PLEXUS CORP - Form 10-Q

Earnings per share:			
Basic		\$ 0.62	\$ 0.45
Diluted		\$ 0.61	\$ 0.44

Table of Contents

For the three months ended January 1, 2011 and January 2, 2010, stock options and stock-settled stock appreciation rights (SARs) related to approximately 1.1 million and 1.4 million shares, respectively, were outstanding but were not included in the computation of diluted earnings per share because the options and stock-settled SARs exercise prices were greater than the average market price of the common shares and, therefore, their effect would be antidilutive.

NOTE 7 - STOCK-BASED COMPENSATION

The Company recognized \$2.4 million and \$1.8 million of compensation expense associated with stock-based awards for the three months ended January 1, 2011 and January 2, 2010, respectively.

The Company continues to use the Black-Scholes valuation model to determine the fair value of stock options and stock-settled SARs. The Company uses the fair value at the date of grant to value restricted stock units and unrestricted stock awards. The Company recognizes the stock-based compensation expense over the stock-based awards vesting period.

NOTE 8 - INCOME TAXES

Income taxes for the three months ended January 1, 2011 and January 2, 2010 were \$0.8 million and \$0.2 million, respectively. The effective tax rates for the three months ended January 1, 2011 and January 2, 2010 were 3 percent and 1 percent, respectively. The increase in the effective tax rate for the current year period compared to the prior year period was primarily due to a change in mix of forecasted earnings in the jurisdictions in which we operate. As demonstrated in recent quarters, the tax rate can vary during the year based on the mix of forecasted earnings by tax jurisdiction. The Company currently benefits from reduced taxes in the Asia Pacific segment due to tax holidays.

As of January 1, 2011, there was no material change in the amount of unrecognized tax benefits recorded for uncertain tax positions. The Company recognizes accrued interest and penalties related to unrecognized tax benefits in income tax expense. The amount of interest and penalties recorded for both the three months ended January 1, 2011 and January 2, 2010 was not material.

It is reasonably possible that a number of uncertain tax positions related to federal and state tax positions may be settled within the next 12 months. Settlement of these matters is not expected to have a material effect on the Company's consolidated results of operations, financial position and cash flows.

The Company maintains valuation allowances when it is more likely than not that all or a portion of a deferred tax asset will not be realized. Despite recent losses in the United States tax jurisdiction, the Company has concluded that it continues to be more likely than not that the net U.S. deferred tax assets will be realized, and no valuation allowance is warranted. If the United States operations continue to generate losses, there may be a need to provide a valuation allowance on our net United States deferred tax assets.

NOTE 9 - BUSINESS SEGMENT, GEOGRAPHIC AND MAJOR CUSTOMER INFORMATION

Reportable segments are defined as components of an enterprise about which separate financial information is available that is evaluated regularly by the chief operating decision maker, or group, in assessing performance and allocating resources.

In the fiscal first quarter of 2011, we completed our migration to a regional reporting structure and as a result modified our reportable segments. See Note 1 in Condensed Consolidated Financial Statements for further information.

The Company uses an internal management reporting system, which provides important financial data to evaluate performance and allocate the Company's resources on a regional basis. Net sales for segments are attributed

Table of Contents

to the region in which the product is manufactured or service is performed. The services provided, manufacturing processes used, class of customers serviced and order fulfillment processes used are similar and generally interchangeable across the segments. A segment's performance is evaluated based upon its operating income (loss). A segment's operating income (loss) includes its net sales less cost of sales and selling and administrative expenses, but excludes corporate and other costs, interest expense, other income (loss), and income taxes. Corporate and other costs primarily represent corporate selling and administrative expenses, and restructuring and impairment costs, if any. These costs are not allocated to the segments, as management excludes such costs when assessing the performance of the segments. Inter-segment transactions are generally recorded at amounts that approximate arm's length transactions. The accounting policies for the regions are the same as for the Company taken as a whole.

Information about the Company's three reportable segments for the three months ended January 1, 2011 and January 2, 2010 were as follows (in thousands):

	Three Months Ended	
	January 1, 2011	January 2, 2010
Net sales:		
AMER	\$ 344,058	\$ 277,444
APAC	272,524	193,126
EMEA	20,088	13,863
Elimination of inter-segment sales	(70,896)	(54,034)
	\$ 565,774	\$ 430,399
Depreciation		
AMER	\$ 3,689	\$ 3,234
APAC	5,222	4,378
EMEA	606	222
Corporate	1,788	1,220
	\$ 11,305	\$ 9,054
Operating income (loss):		
AMER	\$ 18,500	\$ 19,503
APAC	32,681	23,306
EMEA	(279)	(1,187)
Corporate and other costs	(23,053)	(21,400)
	\$ 27,849	\$ 20,222
Capital expenditures:		
AMER	\$ 4,470	\$ 3,574
APAC	6,557	5,010

Edgar Filing: PLEXUS CORP - Form 10-Q

EMEA	1,189	194
Corporate	1,047	3,537
	\$ 13,263	\$ 12,315

	January 1, 2011	October 2, 2010
Total assets:		
AMER	\$ 508,584	\$ 495,639
APAC	578,857	539,543
EMEA	82,478	84,786
Corporate	120,189	170,411
	\$1,290,108	\$1,290,379

Table of Contents

The following enterprise-wide information is provided in accordance with the required segment disclosures. Net sales to unaffiliated customers were based on the Company's location providing product or services (in thousands):

	Three Months Ended	
	January 1, 2011	January 2, 2010
Net sales:		
United States	\$316,242	\$258,849
Malaysia	218,525	170,150
China	53,999	22,976
United Kingdom	19,015	13,782
Mexico	27,816	18,595
Romania	1,073	81
Elimination of inter-segment sales	(70,896)	(54,034)
	\$565,774	\$430,399
	January 1, 2011	October 2, 2010
Long-lived assets:		
United States	\$ 57,594	\$ 59,233
Malaysia	87,268	86,387
China	22,749	21,920
United Kingdom	7,305	7,248
Mexico	9,759	8,655
Romania	4,588	4,484
Corporate	46,305	47,787
	\$235,568	\$235,714

Long-lived assets as of January 1, 2011 and October 2, 2010, exclude other long-term assets totaling \$26.9 million and \$28.7 million, respectively.

The percentages of net sales to customers representing 10 percent or more of total net sales for the indicated periods were as follows:

	Three Months Ended	
	January 1, 2011	January 2, 2010
Juniper Networks, Inc. (Juniper)	17%	17%

No other customers accounted for 10 percent or more of net sales in either period.

NOTE 10 - GUARANTEES

The Company offers certain indemnifications under its customer manufacturing agreements. In the normal course of business, the Company may from time to time be obligated to indemnify its customers or its customers' customers against damages or liabilities arising out of the Company's negligence, misconduct, breach of contract, or infringement of third party intellectual property rights. Certain agreements have extended broader indemnification, and while most agreements have contractual limits, some do not. However, the Company generally does not provide

for such indemnities and seeks indemnification from its customers for damages or liabilities arising out of the

Table of Contents

Company's adherence to customers' specifications or designs or use of materials furnished, or directed to be used, by its customers. The Company does not believe its obligations under such indemnities are material.

In the normal course of business, the Company also provides its customers a limited warranty covering workmanship, and in some cases materials, on products manufactured by the Company. Such warranty generally provides that products will be free from defects in the Company's workmanship and meet mutually agreed-upon specifications for periods generally ranging from 12 months to 24 months. If a product fails to comply with the Company's limited warranty, the Company's obligation is generally limited to correcting, at its expense, any defect by repairing or replacing such defective product. The Company's warranty generally excludes defects resulting from faulty customer-supplied components, design defects or damage caused by any party or cause other than the Company.

The Company provides for an estimate of costs that may be incurred under its limited warranty at the time product revenue is recognized and establishes additional reserves for specifically identified product issues. These costs primarily include labor and materials, as necessary, associated with repair or replacement and are included in the Company's accompanying Condensed Consolidated Balance Sheets in other current accrued liabilities. The primary factors that affect the Company's warranty liability include the value and the number of shipped units and historical and anticipated rates of warranty claims. As these factors are impacted by actual experience and future expectations, the Company assesses the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary.

Below is a table summarizing the activity related to the Company's limited warranty liability for fiscal 2010 and for the three months ended January 1, 2011 (in thousands):

Limited warranty liability, as of October 3, 2009	\$	4,470
Accruals for warranties issued during the period		557
Settlements (in cash or in kind) during the period		(972)
Limited warranty liability, as of October 2, 2010		4,055
Accruals for warranties issued during the period		91
Settlements (in cash or in kind) during the period		(277)
Limited warranty liability, as of January 1, 2011	\$	3,869

NOTE 11 - LITIGATION

In the fiscal fourth quarter of 2010, the Company determined it would incur up to approximately \$1.1 million relating to non-conforming inventory received from a supplier. The Company reached a settlement with the supplier during the fiscal first quarter of 2011 and recorded the \$0.8 million recovery in selling and administrative expenses.

In the fiscal first quarter of 2010, the Company received settlement funds of approximately \$3.2 million related to a court case in which the Company was a plaintiff. The settlement related to prior purchases of inventory and therefore was recorded in cost of sales.

The Company is party to certain other lawsuits in the ordinary course of business. Management does not believe that these proceedings, individually or in the aggregate, will have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

NOTE 12 - CONTINGENCIES

We were notified in April 2009 by U.S. Customs and Border Protection (CBP) of its intention to conduct a customary Focused Assessment of our import activities during fiscal 2008 and of our processes and procedures to comply with U.S. Customs laws and regulations. We recorded an accrual in Other Accrued current liabilities at the time the amount became estimable and probable, which was not material to the financial statements. During September 2010, the Company reported errors relating to import trade activity from July 2004 to the date of Plexus

Table of Contents

report. The Company is currently awaiting final determination of CBP duties and fees. Plexus has agreed that it will implement improved processes and procedures and review these corrective measures with CBP. At this time, we do not believe that any deficiencies in processes or controls or unanticipated costs, unpaid duties or penalties associated with this matter will have a material adverse effect on Plexus or the Company's consolidated financial position, results of operations or cash flows.

NOTE 13 - NEW ACCOUNTING PRONOUNCEMENTS

In October 2009, the FASB issued new accounting guidance for Multiple-Deliverable Revenue Arrangements, which establishes a selling price hierarchy for determining the selling price of a deliverable, replaces the term "fair value" in the revenue allocation guidance with "selling price," eliminates the residual method of allocation by requiring that arrangement consideration be allocated at the inception of the arrangement to all deliverables using the relative selling price method and requires that a vendor determine its best estimate of selling price in a manner that is consistent with that used to determine the price to sell the deliverable on a stand-alone basis. The Company adopted this guidance beginning October 3, 2010, and the adoption did not have a material effect on our financial position, results of operations, or cash flows.

In June 2009, the FASB issued an amendment to the accounting and disclosure requirements for the consolidation of variable interest entities (VIEs). The elimination of the concept of a qualifying special-purpose entity (QSPE) removes the exception from applying the consolidation guidance within this amendment. This amendment requires an enterprise to perform a qualitative analysis when determining whether or not it must consolidate a VIE. The amendment also requires an enterprise to continuously reassess whether it must consolidate a VIE. Additionally, the amendment requires enhanced disclosures about an enterprise's involvement with VIEs and any significant change in risk exposure due to that involvement, as well as how its involvement with VIEs impacts the enterprise's financial statements. Finally, an enterprise will be required to disclose significant judgments and assumptions used to determine whether or not to consolidate a VIE. The Company adopted this amendment beginning October 3, 2010, and the adoption did not have a material effect on our financial position, results of operations, or cash flows.

Table of Contents

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

SAFE HARBOR CAUTIONARY STATEMENT UNDER THE PRIVATE SECURITIES LITIGATION REFORM ACT OF 1995:

The statements contained in this Form 10-Q that are not historical facts (such as statements in the future tense and statements including believe, expect, intend, plan, anticipate, goal, target and similar terms and concepts) including all discussions of periods which are not yet completed, are forward-looking statements that involve risks and uncertainties, including, but not limited to:

the economic performance of the industries, sectors and customers we serve

the risk of customer delays, changes, cancellations or forecast inaccuracies in both ongoing and new programs

the continuing poor visibility of future orders, particularly in view of current economic conditions

the effects of the volume of revenue from certain sectors or programs on our margins in particular periods

our ability to secure new customers, maintain our current customer base and deliver product on a timely basis

the risk that our revenue and/or profits associated with customers who are acquired by third parties will be negatively affected

the particular risks relative to new customers, including our arrangements with The Coca-Cola Company, which risks include customer and other delays, start-up costs, the potential inability to execute, the establishment of appropriate terms of agreements and the lack of a track record of order volume and timing

the risks of concentration of work for certain customers

our ability to successfully manage a complex business model characterized by high customer and product mix, low volumes and demanding quality, regulatory and other requirements

the risk that new program wins and/or customer demand may not result in the expected revenue or profitability

the fact that customer orders may not lead to long-term relationships

raw material and component cost fluctuations particularly due to sudden increases in customer demand

the risks associated with excess and obsolete inventory, including the risk that inventory purchased on behalf of our customers may not be consumed or otherwise paid for by customers, resulting in an inventory write-off

the weakness of the global economy and the continuing instability of the global financial markets and banking system, including the potential inability of our customers or suppliers to access credit facilities

the effect of changes in the pricing and margins of products

the effect of start-up costs of new programs and facilities, including our recent and planned expansions, such as our new replacement facility in Oradea, Romania, and our plans to further expand in Penang, Malaysia, Darmstadt, Germany, Xiamen, China and other locations

the risks associated with having significant operations and planned growth in countries outside the United States, including the effects of international political developments, economic or political instability, or foreign exchange rate fluctuations

the risk of unanticipated costs, unpaid duties and penalties related to an ongoing audit of our import compliance by U.S. Customs and Border Protection

possible unexpected costs and operating disruption in transitioning programs

the potential effect of fluctuations in the value of the currencies in which we transact business

the potential effect of world or local events or other events outside our control (such as drug cartel-related violence in Mexico, changes in oil prices, terrorism and war in the Middle East)

the impact of increased competition, and

other risks detailed herein, as well as in our Securities and Exchange Commission filings (particularly in Part I, Item 1A of our annual report on Form 10-K for the fiscal year ended October 2, 2010).

Table of Contents**OVERVIEW**

The following information should be read in conjunction with our condensed consolidated financial statements included herein and the Risk Factors section in Part I, Item 1A of our annual report on Form 10-K for the fiscal year ended October 2, 2010.

Plexus Corp. and its subsidiaries (together Plexus, the Company, or we) participate in the Electronic Manufacturing Services (EMS) industry. We deliver optimized Product Realization solutions through a unique Product Realization Value Stream service model. This customer focused service model seamlessly integrates innovative product design, customized supply chain solutions, uniquely configured focused factory manufacturing, global end-market fulfillment and after-market services to deliver comprehensive end-to-end solutions for customers. We provide these services to original equipment manufacturers (OEMs) and other technology companies in the wireline/networking, wireless infrastructure, medical, industrial/commercial and defense/security/aerospace market sectors. We provide advanced product development, manufacturing and testing services to our customers with a focus on the mid-to-lower-volume, higher complexity segment of the EMS market. Our customers products typically require exceptional production and supply-chain flexibility, necessitating an optimized demand-pull-based manufacturing and supply chain solution across an integrated global platform. Many of our customers products require complex configuration management and direct order fulfillment to their customers across the globe. In such cases we provide global logistics management and after-market service and repair. Our customers products may have stringent requirements for quality, reliability and regulatory compliance. We offer our customers the ability to outsource all phases of product realization, including product specifications; development, design and design verification; regulatory compliance support; prototyping and new product introduction; manufacturing test equipment development; materials sourcing, procurement and supply-chain management; product assembly/manufacturing, configuration and test; order fulfillment, logistics and service/repair.

Plexus is passionate about its goal to be the best EMS company in the world at providing services for customers that have mid-to-lower-volume requirements and a higher complexity of products. We have tailored our engineering services, manufacturing operations, supply-chain management, workforce, business intelligence systems, financial goals and metrics specifically to support these types of programs. Our flexible manufacturing facilities and processes are designed to accommodate customers with multiple product-lines and configurations as well as unique quality and regulatory requirements. Each of these customers is supported by a multi-disciplinary customer team and one or more uniquely configured focus factories supported by a supply-chain and logistics solution specifically designed to meet the flexibility and responsiveness required to support that customer s fulfillment requirements.

Our go-to-market strategy is also tailored to our target market sectors and business strategy. We have business development and customer management teams that are dedicated to each of the five sectors we serve. These teams are accountable for understanding the sector participants, technology, unique quality and regulatory requirements and longer-term trends in these sectors. Further, these teams help set our strategy for growth in these sectors with a particular focus on expanding the services and value-add that we provide to our current customers while strategically targeting select new customers to add to our portfolio.

Our financial model is aligned with our business strategy, with our primary focus to earn a return on invested capital (ROIC) in excess of our weighted average cost of capital (WACC). The smaller volumes, flexibility requirements and fulfillment needs of our customers typically result in greater investments in inventory than many of our competitors, particularly those that provide EMS services for high-volume, less complex products with less stringent requirements (such as consumer electronics). In addition, our cost structure relative to these peers includes higher investments in selling and administrative costs as a percentage of sales to support our sector-based go-to-market strategy, smaller program sizes, flexibility, and complex quality and regulatory compliance requirements. By exercising discipline to generate a ROIC in excess of our WACC, our goal is to ensure that Plexus creates a value proposition for our shareholders as well as our customers.

Our customers include both industry-leading OEMs and other technology companies that have never manufactured products internally. As a result of our focus on serving market sectors that rely on advanced electronics technology, our business is influenced by technological trends such as the level and rate of development of telecommunications infrastructure, the expansion of networks and use of the Internet. In addition, the federal Food and

Drug Administration's approval of new medical devices, defense procurement practices and other

Table of Contents

governmental approval and regulatory processes can affect our business. Our business has also benefited from the trend to increased outsourcing by OEMs.

We provide most of our contract manufacturing services on a turnkey basis, which means that we procure some or all of the materials required for product assembly. We provide some services on a consignment basis, which means that the customer supplies the necessary materials, and we provide the labor and other services required for product assembly. Turnkey services require material procurement and warehousing, in addition to manufacturing, and involve greater resource investments than consignment services. Other than certain test equipment and software used for internal operations, we do not design or manufacture our own proprietary products.

EXECUTIVE SUMMARY

As a consequence of the Company's use of a 4-4-5 weekly accounting system, periodically an additional week must be added to the fiscal year to re-align with a fiscal year end at the Saturday closest to September 30. The accounting periods for the three months ended January 1, 2011 and January 2, 2010 each included 91 days.

In the fiscal first quarter of 2011, we completed our migration to a regional reporting structure. This change included establishing regional targets for various financial metrics, delegating additional authority to the regions to manage their business, and changing our related internal reporting. Given this change to regional reporting and management as well as in the information used by management for assessing performance and allocating Company resources, we modified our reporting segments. Prior to fiscal 2011, the Company's reportable segments consisted of the United States, Asia, Europe and Mexico. We have combined our United States and Mexico segments into the

Americas (AMER) segment and renamed our Asia segment Asia Pacific (APAC) and our Europe segment Europe, Middle East and Africa (EMEA) to better represent our long-range regional focus. As a result, we have conformed all prior period segment presentations to be consistent with our current reportable segments.

Three months ended January 1, 2011. Net sales for the three months ended January 1, 2011, of \$565.8 million increased by \$135.4 million, or 31.5 percent, as compared to the three months ended January 2, 2010. The net sales increase in the current year period was driven primarily by higher end-market demand from numerous existing customers in each of our market sectors, as well as the addition of a new customer in the wireless infrastructure sector. Net sales to Juniper Networks, Inc. (Juniper), our largest customer, increased as a result of improved end-market demand for the mix of Juniper products we produce.

Gross margins were 9.7 percent for the three months ended January 1, 2011, which compared unfavorably to 10.3 percent for the three months ended January 2, 2010. The prior year period benefited from approximately \$3.2 million of proceeds from a litigation settlement. Excluding the prior year settlement, the gross margin percentage would have increased slightly over the prior year as a result of increased net sales and the mix of customer revenue, partially offset by an increase in fixed expenses primarily due to higher headcount to support revenue growth.

Selling and administrative expenses for the three months ended January 1, 2011 were \$27.1 million, an increase of \$2.7 million, or 11.3 percent, over the three months ended January 2, 2010. The current year period increase was primarily related to higher headcount to support revenue growth and increased stock based compensation expense, offset by funds from a dispute recovery and lower variable incentive compensation expense.

Net income for the three months ended January 1, 2011 increased by \$7.2 million to \$25.0 million from the three months ended January 2, 2010 and diluted earnings per share increased to \$0.61 in the current year period from \$0.44 in the prior year period. Net income increased due to higher sales, partially offset by increased fixed and selling and administrative expenses primarily as a result of increased headcount to support the revenue growth. The effective tax rate in the current year period was 3 percent as compared to 1 percent in the prior year period. The increase in the effective tax rate for the current year period as compared to the prior year period was primarily due to a change in mix of forecasted earnings in the jurisdictions in which we operate. As demonstrated in recent quarters, the tax rate can vary during the year based on the mix of forecasted earnings by tax jurisdiction. We currently benefit from reduced taxes in the Asia Pacific segment due to tax holidays.

Table of Contents

Fiscal 2011 outlook. Our current expectations for fiscal 2011 include meaningful challenges, particularly in the third quarter, due to a confluence of issues. These issues include the winding down of two significant manufacturing programs for customers that were acquired during the past year and will transition out of Plexus, a fairly broad-based reduction in customer forecasts and a significant production delay in the two programs for The Coca-Cola Company. As a consequence, we expect some volatility among the remaining quarters of the fiscal year with fiscal 2011 full year anticipated revenue growth in the range of 10-13% over the prior fiscal year.

Based on customer forecasts and current economic conditions, we currently expect net sales in the second quarter of fiscal 2011 to be in the range of \$540 million to \$570 million; however, our results will ultimately depend upon the actual level of customer orders and production. The second quarter will be unfavorably impacted by the three issues discussed above, as well as by an increase in the structural seasonal operating costs, including salary adjustments, which need to be absorbed by the financial model going forward. Assuming that net sales are in the range noted above, we would currently expect to earn, before any restructuring and impairment costs, between \$0.53 to \$0.58 per diluted share in the second quarter of fiscal 2011.

We currently expect the annual effective tax rate for fiscal 2011 to be 3%.

RESULTS OF OPERATIONS

Net sales. Net sales for the indicated periods were as follows (dollars in millions):

	Three months ended		Increase / (Decrease)	
	January 1, 2011	January 2, 2010		
Net Sales	\$565.8	\$430.4	\$135.4	31.5%

For the three months ended January 1, 2011, our net sales increase of 31.5 percent was the result of higher net sales in all market sectors due to improved end-market demand from numerous existing customers, as well as the addition of new customers in the wireless infrastructure, medical, and industrial/commercial sectors. Net sales to Juniper increased as a result of improved end-market demand for the mix of Juniper products we produce.

Our percentages of net sales by market sector for the indicated periods were as follows:

<u>Market Sector</u>	Three months ended	
	January 1, 2011	January 2, 2010
Wireline/Networking	41%	47%
Wireless Infrastructure	10%	11%
Medical	21%	18%
Industrial/Commercial	21%	15%
Defense/Security/Aerospace	7%	9%

The percentages of net sales to customers representing 10 percent or more of net sales and net sales to our ten largest customers for the indicated periods were as follows:

	Three months ended	
	January 1, 2011	January 2, 2010
Juniper	17%	17%
Top 10 customers	56%	62%

Table of Contents

Net sales to our largest customers may vary from time to time depending on the size and timing of customer program commencements, terminations, delays, modifications and transitions. We remain dependent on continued sales to our significant customers, and we generally do not obtain firm, long-term purchase commitments from our customers. Customers' forecasts can and do change as a result of changes in their end-market demand and other factors, including global economic conditions. Any material change in forecasts or orders from these major accounts, or other customers, could materially affect our results of operations, as discussed above in our fiscal 2011 outlook. In addition, as our percentage of net sales to customers in a specific sector becomes larger relative to other sectors, we will become increasingly dependent upon the economic and business conditions affecting that sector.

In the current economic environment, we are seeing increased merger and acquisition activity that has already impacted, and may continue to impact, our customers. Specifically, two of our customers were acquired in the first quarter of fiscal 2010. Our production for these two customers is ramping down during the first half of fiscal 2011 and full disengagement of both customers is expected by the end of the fiscal year.

Gross profit. Gross profit and gross margins for the indicated periods were as follows (dollars in millions):

	Three months ended		Increase / (Decrease)	
	January 1, 2011	January 2, 2010		
Gross Profit	\$54.9	\$44.5	\$ 10.4	23.3%
Gross Margin	9.7%	10.3%		

For the three months ended January 1, 2011, gross profit was impacted by the following factors:
increased capacity utilization from higher revenue levels in the current year period

increased fixed expenses in the current year period, primarily in the Americas and Asia Pacific reportable segments, due to higher headcount expense of approximately \$6.6 million to support the revenue growth

a \$3.2 million benefit in the fiscal first quarter of 2010 from a litigation settlement.

Gross margins reflect a number of factors that can vary from period to period, including product and service mix, the level of new facility start-up costs, inefficiencies resulting from the transition of new programs, product life cycles, sales volumes, price reductions, overall capacity utilization, labor costs and efficiencies, the management of inventories, component pricing and shortages, fluctuations and timing of customer orders, changing demand for our customers' products and competition within the electronics industry. During fiscal 2010, we were in a constrained supply environment, which caused periods of parts shortages and delays for some components, based on lack of capacity at some of our suppliers to meet increased demand from the gradually improving economic outlook. Such shortages and delays could negatively impact net sales, inventory levels, component costs and margin. Additionally, turnkey manufacturing involves the risk of inventory management, and a change in component costs can directly impact average selling prices, gross margins and net sales. Although we focus on maintaining gross margins, there can be no assurance that gross margins will not decrease in future periods.

Design work performed by the Company is not the proprietary property of Plexus and substantially all costs incurred with this work are considered reimbursable by our customers. We do not track research and development costs that are not reimbursed by our customers and we consider these amounts immaterial.

Selling and administrative expenses. Selling and administrative expenses (S&A) for the indicated periods were as follows (dollars in millions):

	Three months ended		Increase / (Decrease)	
	January 1, 2011	January 2, 2010		
S&A	\$27.1	\$24.3	\$ 2.7	11.3%

Edgar Filing: PLEXUS CORP - Form 10-Q

Percent of net sales

4.8%

5.7%

21

Table of Contents

For the three months ended January 1, 2011, the dollar increase in S&A was due primarily to an increase in headcount expense of approximately \$2.9 million to support the higher revenue achieved during the fiscal first quarter of 2011, as well as increased stock-based compensation expense of approximately \$0.4 million, partially offset by a dispute recovery of approximately \$0.8 million and lower variable incentive compensation expense of approximately \$0.2 million.

Income taxes. Income taxes for the indicated periods were as follows (dollars in millions):

	Three months ended	
	January 1, 2011	January 2, 2010
Income tax expense	\$0.8	\$0.2
Effective tax rate	3%	1%

The change in effective tax rate for the three months ended January 1, 2011, as compared to the three months ended January 2, 2010, was primarily due to a change in mix of forecasted earnings in the jurisdictions in which we operate. As demonstrated in recent quarters, the tax rate can vary during the year based on the mix of forecasted earnings by tax jurisdiction. We currently benefit from reduced taxes in the Asia Pacific segment due to tax holidays.

Our net deferred income tax assets as of January 1, 2011, reflect a \$1.6 million valuation allowance against certain deferred income taxes and a remaining valuation allowance of \$1.0 million related to tax deductions associated with stock-based compensation. If the United States operations continue to generate losses, there may be a need to provide a valuation allowance on our net United States deferred tax assets.

We currently expect the annual effective tax rate for fiscal 2011 to be 3%.

LIQUIDITY AND CAPITAL RESOURCES

Operating Activities. Cash flows used in operating activities were \$21.1 million for the three months ended January 1, 2011, as compared to cash flows used in operating activities of \$10.3 million for the three months ended January 2, 2010. During the three months ended January 1, 2011, cash flows used by operating activities were primarily the result of increased inventory and accounts receivable as well as decreased accounts payable and accrued liabilities, offset in part by earnings after adjusting for the non-cash effects of depreciation, amortization and stock-based compensation expenses.

Inventory levels increased in the fiscal first quarter of 2011 to support new customers that are ramping in the fiscal second quarter, customer demand variability with our existing customers and some inventory that did not ship at the end of the quarter due to component shortages. Inventory turns decreased to 3.9 as of January 1, 2011, from 4.1 turns for the fiscal year ended October 2, 2010. Days in inventory changed unfavorably as of January 1, 2011 to 93 days compared to 90 days as of October 2, 2010 due to the factors discussed above. We are taking steps to actively manage these inventory levels down, with the assistance of our customers.

The overall increase in accounts receivable was mainly due to higher net sales for the three months ended January 1, 2011, as compared to the prior year. As of January 1, 2011, quarterly days sales outstanding in accounts receivable were 52 days as compared to the 51 days for the fiscal year ended October 2, 2010 and were impacted by the timing of shipments during the quarter.

The increase in accounts payable was largely the result of the timing of inventory receipts, which were concentrated in the early portion of the quarter for the three months ended January 1, 2011, as compared to the prior year.

Investing Activities. Cash flows used in investing activities totaled \$13.2 million for the three months ended January 1, 2011, and were primarily for additions to property, plant and equipment in the Americas and Asia Pacific.

Table of Contents

These investments were for new equipment to support customer demand as well as capacity investments in both Penang, Malaysia and Xiamen, China. See Note 9 in Notes to Condensed Consolidated Financial Statements for further information regarding our capital expenditures by reportable segment.

We utilized available cash and operating cash flows as the sources for funding our operating requirements. We currently estimate capital expenditures for fiscal 2011 to be approximately \$100 million. A significant portion of the fiscal 2011 capital expenditures is anticipated to be used for the construction of new manufacturing facilities in Penang, Malaysia and Xiamen, China, as mentioned above.

Financing Activities. Cash flows used in financing activities totaled \$4.5 million for the three months ended January 1, 2011, as compared to cash flows used of \$2.1 million for the three months ended January 2, 2010. Cash flows used in the current year period represented payments on our outstanding term loan described below, partially offset by cash generated from exercises of stock options.

On April 4, 2008, we entered into our Credit Facility with a group of banks which allows us to borrow \$150 million in term loans and \$100 million in revolving loans. The \$150 million in term loans was immediately funded and the \$100 million revolving credit facility is currently available. The Credit Facility is unsecured and may be increased by an additional \$100 million (the accordion feature) if we have not previously terminated all or any portion of the Credit Facility, there is no event of default existing under the credit agreement and both we and the administrative agent consent to the increase. The Credit Facility expires on April 4, 2013. Borrowings under the Credit Facility may be either through term loans, revolving or swing loans or letter of credit obligations. As of January 1, 2011, we had term loan borrowings of \$108.8 million outstanding and no revolving borrowings under the Credit Facility.

The Credit Facility contains certain financial covenants, which include a maximum total leverage ratio, maximum value of fixed rentals and operating lease obligations, a minimum interest coverage ratio and a minimum net worth test, all as defined in the agreement. As of January 1, 2011, we were in compliance with all debt covenants. If we incur an event of default, as defined in the Credit Facility (including any failure to comply with a financial covenant), the group of banks has the right to terminate the Credit Facility and all other obligations, and demand immediate repayment of all outstanding sums (principal and accrued interest). The interest rate on the borrowing varies depending upon our then-current total leverage ratio; as of January 1, 2011, the Company could elect to pay interest at a defined base rate or the LIBOR rate plus 1.00%. Rates would increase upon negative changes in specified Company financial metrics and would decrease upon reduction in the current total leverage ratio to no less than LIBOR plus 1.00%. We are also required to pay an annual commitment fee on the unused credit commitment based on our leverage ratio; the current fee is 0.25%. Unless the accordion feature is exercised, this fee applies only to the initial \$100 million of availability (excluding the \$150 million of term borrowings). Origination fees and expenses associated with the Credit Facility totaled approximately \$1.3 million and have been deferred. These origination fees and expenses will be amortized over the five year term of the Credit Facility. Quarterly principal repayments on the term loan of \$3.75 million per quarter began on June 30, 2008 and end on April 4, 2013, with a final balloon repayment of \$75.0 million.

The Credit Facility allows for the future payment of cash dividends or the future repurchases of shares provided that no event of default (including any failure to comply with a financial covenant) is existing at the time of, or would be caused by, the dividend payment or the share repurchases.

In June 2008, the Company entered into three interest rate swap contracts related to the \$150 million in term loans under the Credit Facility that had an initial notional value of \$150 million and mature on April 4, 2013. The total fair value of these interest rate swap contracts was \$7.7 million as of January 1, 2011. As of January 1, 2011, the total combined notional amount of the Company's three interest rate swaps was \$108.8 million.

Our Malaysian operations have entered into forward exchange contracts on a rolling basis with a total notional value of \$41.0 million as of January 1, 2011. These forward contracts will fix the exchange rates on foreign currency cash used to pay a portion of our local currency expenses. The changes in the fair value of the forward contracts are recorded in Accumulated other comprehensive income on the accompanying Condensed Consolidated Balance Sheets until earnings are affected by the variability of cash flows. The total fair value of the forward contracts was \$2.0 million at January 1, 2011.

Table of Contents

As of January 1, 2011, we held \$2.0 million of auction rate securities maturing on March 17, 2042, which were classified as other long-term assets and whose underlying assets are in guaranteed student loans that are backed by a U. S. government agency. If the credit quality deteriorates for these adjustable rate securities, we may in the future be required to record an impairment charge on these investments. The fair value of the auction rate securities approximates the carrying value of \$2.0 million as of January 1, 2011. We believe that these securities are marketable.

Based on current expectations, we believe that our projected cash flows from operations, available cash and short-term investments, the Credit Facility, and our leasing capabilities should be sufficient to meet our working capital and fixed capital requirements for the next twelve months. \$100 million of committed credit is currently available under the Credit Facility, with another \$100 million available in an accordion facility, which is contingent upon compliance with the terms of the Credit Agreement and lender approval. If our future financing needs increase, we may need to arrange additional debt or equity financing. Accordingly, we evaluate and consider from time to time various financing alternatives to supplement our financial resources.

We have not paid cash dividends in the past and do not currently anticipate paying them in the future. However, the company evaluates from time to time potential uses of excess cash, which in the future may include share repurchases, a special dividend or recurring dividends.

REPORTABLE SEGMENTS

In the fiscal first quarter of 2011, we completed our migration to a regional reporting structure and as a result made a minor change to our reportable segments. See Executive Summary above for further information.

A further discussion of financial performance by reportable segment is presented below (dollars in millions):

	Three Months Ended	
	January 1, 2011	January 2, 2010
Net sales:		
AMER	\$344.0	\$277.5
APAC	272.5	193.1
EMEA	20.1	13.9
Elimination of inter-segment sales	(70.8)	(54.1)
	\$565.8	\$430.4

	Three Months Ended	
	January 1, 2011	January 2, 2010
Operating income (loss):		
AMER	\$ 18.5	\$ 19.5
APAC	32.7	23.3
EMEA	(0.3)	(1.2)
Corporate and other costs	(23.1)	(21.4)
	\$ 27.8	\$ 20.2

Americas (AMER): Net sales for the three months ended January 1, 2011 increased \$66.5 million, or 24.0 percent, due to higher end-market demand from numerous existing customers in each of our market sectors along with demand from new customers in the wireless infrastructure and medical sectors, partially offset by the disengagement of a wireline/networking customer. Net sales to our largest customer, Juniper, increased compared to the prior year period due to higher end-market demand for the mix of Juniper products we produce. Operating income for the current year period decreased due to the prior year period benefitting

Table of Contents

from a \$3.2 million litigation settlement as well as higher fixed expenses, including approximately \$2.8 million of greater employee headcount to support the revenue growth.

Asia Pacific (APAC): Net sales for the three months ended January 1, 2011 increased \$79.4 million, or 41.1 percent, due to higher end-market demand from numerous existing customers, primarily in our wireline/networking and medical sectors, as well as increased demand from a new customer in the industrial/commercial sector. Net sales to Juniper increased as a result of improved end-market demand for the mix of Juniper products we produce. Operating income in the current year period improved as a result of the net sales growth.

Europe, Middle East, Africa (EMEA): Net sales for the three months ended January 1, 2011 increased \$6.2 million, or 44.6 percent, due primarily to increased demand from two existing customer programs in the industrial/commercial sector. Operating loss in the current year period decreased \$0.9 million as compared to the prior year period due to the revenue growth in the existing United Kingdom facility, partially offset by operating costs from our Romania facility.

For our significant customers, we generally manufacture product in more than one location. For example, net sales to Juniper, our largest customer, occur in the Americas and Asia Pacific segments. See Note 9 in Notes to Condensed Consolidated Financial Statements for certain financial information regarding our reportable segments, including detail of net sales by reportable segment.

CONTRACTUAL OBLIGATIONS, COMMITMENTS AND OFF-BALANCE SHEET OBLIGATIONS

Our disclosures regarding contractual obligations and commercial commitments are located in various parts of our regulatory filings. Information in the following table provides a summary of our contractual obligations and commercial commitments as of January 1, 2011 (dollars in millions):

<u>Contractual Obligations</u>	Total	Payments Due by Fiscal Period			2016 and thereafter
		Remaining in 2011	2012-2013	2014-2015	
Long-Term Debt Obligations (1)	\$ 120.8	\$ 15.7	\$ 105.1	\$ -	\$ -
Capital Lease Obligations	22.0	2.7	7.7	8.0	3.6
Operating Lease Obligations	39.4	6.9	15.7	10.8	6.0
Purchase Obligations (2)	385.5	375.0	9.6	0.4	0.5
Other Long-Term Liabilities on the Balance Sheet (3)	9.1	0.8	1.5	1.5	5.3
Other Long-Term Liabilities not on the Balance Sheet (4)	6.2	4.2	2.0	-	-
Total Contractual Cash Obligations	\$583.0	\$ 405.3	\$ 141.6	\$ 20.7	\$ 15.4

(1) - As of April 4, 2008, we entered into the Credit Facility and immediately funded a term loan for \$150 million. The amounts listed above include interest, as we intend to hold the loan to maturity. See Note 4 in Notes to Condensed Consolidated Financial Statements for further information.

(2) - As of January 1, 2011, purchase obligations consist of purchases of inventory and equipment in the ordinary course of business.

(3) - As of January 1, 2011, other long-term obligations on the balance sheet included deferred compensation obligations to certain of our former and current executive officers, as well as other key employees, and an asset retirement obligation. We have excluded from the table the impact, as of January 1, 2011, of approximately \$5.2 million related to unrecognized income tax benefits. The Company cannot make reliable estimates of the future cash flows by period related to this obligation.

Table of Contents

(4) - As of January 1, 2011, other long-term obligations not on the balance sheet consisted of a commitment for salary continuation in the event employment of one executive officer of the Company is terminated without cause as well as a subsequent commitment for approximately \$3.4 million related to an acquisition of land. We did not have, and were not subject to, any lines of credit, standby letters of credit, guarantees, standby repurchase obligations, other off-balance sheet arrangements or other commercial commitments that are material.

DISCLOSURE ABOUT CRITICAL ACCOUNTING POLICIES

Our accounting policies are disclosed in our 2010 annual report on Form 10-K. During the first quarter of fiscal 2011, there were no material changes to these policies.

NEW ACCOUNTING PRONOUNCEMENTS

See Note 13 in Notes to Condensed Consolidated Financial Statements for further information regarding new accounting pronouncements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to market risk from changes in foreign exchange and interest rates. We selectively use financial instruments to reduce such risks.

Foreign Currency Risk

We do not use derivative financial instruments for speculative purposes. Our policy is to selectively hedge our foreign currency denominated transactions in a manner that partially offsets the effects of changes in foreign currency exchange rates. We typically use foreign currency contracts to hedge only those currency exposures associated with certain assets and liabilities denominated in non-functional currencies. Corresponding gains and losses on the underlying transaction generally offset the gains and losses on these foreign currency hedges. Beginning in July 2009, we entered into forward contracts to hedge a portion of our foreign currency denominated transactions in our Asia Pacific reportable segment, as described in Note 5 in Notes to Condensed Consolidated Financial Statements. Our international operations create potential foreign exchange risk. Our percentages of transactions denominated in currencies other than the U.S. dollar for the indicated periods were as follows:

	Three months ended	
	January 1, 2011	January 2, 2010
Net Sales	5%	4%
Total Costs	13%	12%

The Company has evaluated the potential foreign currency exchange rate risk on transactions denominated in currencies other than the U.S. Dollar for the periods presented above. Based on the Company's overall currency exposure, as of January 1, 2011, a 10 percent change in the value of the U.S. Dollar relative to our other transactional currencies would not have a material effect on the Company's financial position, results of operations, or cash flows.

Interest Rate Risk

We have financial instruments, including cash equivalents and short-term investments, which are sensitive to changes in interest rates. We consider the use of interest-rate swaps based on existing market conditions and have entered into interest rate swaps for \$108.8 million in term loans, as described in Note 5 in Notes to Condensed Consolidated Financial Statements. As with any agreement of this type, our interest rate swap agreements are subject to the further risk that the counterparties to these agreements may fail to comply with their obligations thereunder.

Table of Contents

The primary objective of our investment activities is to preserve principal, while maximizing yields without significantly increasing market risk. To achieve this, we maintain our portfolio of cash equivalents and short-term investments in a variety of highly rated securities, money market funds and certificates of deposit and limit the amount of principal exposure to any one issuer.

Our only material interest rate risk is associated with our Credit Facility under which we borrowed \$150 million. Through the use of interest rate swaps, as described above, we have fixed the basis on which we pay interest, thus eliminating much of our interest rate risk. A 10 percent change in the weighted average interest rate on our average long-term borrowings would have had only a nominal impact on net interest expense for both the three months ended January 1, 2011 and January 2, 2010, respectively.

Auction Rate Securities

As of January 1, 2011, we held \$2.0 million of auction rate securities maturing on March 17, 2042, which were classified as long-term other assets and whose underlying assets are in guaranteed student loans backed by a U.S. government agency. If the credit quality deteriorates for these adjustable rate securities, we may in the future be required to record an impairment charge on these investments. The fair value of the auction rate securities approximates the carrying value of \$2.0 million as of January 1, 2011. We believe that these securities are marketable.

ITEM 4. CONTROLS AND PROCEDURES

Disclosure Controls and Procedures: The Company maintains disclosure controls and procedures designed to ensure that the information the Company must disclose in its filings with the Securities and Exchange Commission (SEC) is recorded, processed, summarized and reported on a timely basis. The Company s principal executive officer and principal financial officer have reviewed and evaluated, with the participation of the Company s management, the Company s disclosure controls and procedures as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act) as of the end of the period covered by this report (the Evaluation Date). Based on such evaluation, the chief executive officer and chief financial officer have concluded that, as of the Evaluation Date, the Company s disclosure controls and procedures are effective (a) in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by the Company in the reports the Company files or submits under the Exchange Act, and (b) in assuring that information is accumulated and communicated to the Company s management, including the chief executive officer and chief financial officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control Over Financial Reporting: During the first quarter of fiscal 2011, there have been no changes to the Company s internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that have materially affected, or are reasonably likely to materially affect, the Company s internal control over financial reporting.

Limitations on the Effectiveness of Controls: Our management, including our chief executive officer and chief financial officer, does not expect that our disclosure controls and internal controls will prevent all errors and all fraud. 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 the 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 the individual acts of some persons, by collusion of two or more people, or by management override of 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. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Notwithstanding the foregoing limitations on the effectiveness of controls, we have nonetheless reached the conclusion that the Company s disclosure controls and procedures are effective at the reasonable assurance level.

Table of Contents**PART II. OTHER INFORMATION****ITEM 1. Legal Proceedings**

We were notified in April 2009 by U.S. Customs and Border Protection (CBP) of its intention to conduct a customary Focused Assessment of our import activities during fiscal 2008 and of our processes and procedures to comply with U.S. Customs laws and regulations. We recorded an accrual in Other Accrued current liabilities at the time the amount became estimable and probable, which was not material to the financial statements. During September 2010 the Company reported errors relating to import trade activity from July 2004 to the date of Plexus report. The Company is currently awaiting final determination of CBP duties and fees. Plexus has agreed that it will implement improved processes and procedures and review these corrective measures with CBP. At this time, we do not believe that any deficiencies in processes or controls or unanticipated costs, unpaid duties or penalties associated with this matter will have a material adverse effect on Plexus or the Company's consolidated financial position, results of operations or cash flows.

The Company is party to certain other lawsuits in the ordinary course of business. Management does not believe that these proceedings, individually or in the aggregate, will have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

ITEM 1A. Risk Factors

In addition to the risks and uncertainties discussed herein, particularly those discussed in the Safe Harbor Cautionary Statement, Fiscal 2011 outlook and the other sections of Management's Discussion and Analysis of Financial Condition and Results of Operations in Part I, Item 2, see the risk factors set forth in Part I, Item 1A of the Company's annual report on Form 10-K for the fiscal year ended October 2, 2010.

ITEM 6. Exhibits

- 31.1 Certification of Chief Executive Officer pursuant to Section 302(a) of the Sarbanes Oxley Act of 2002.
- 31.2 Certification of Chief Financial Officer pursuant to Section 302(a) of the Sarbanes Oxley Act of 2002.
- 32.1 Certification of the CEO pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification of the CFO pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101 The following materials from Plexus Corp.'s Quarterly Report on Form 10-Q for the quarter ended January 1, 2011, formatted in XBRL (Extensible Business Reporting Language): (i) the Condensed Consolidated Statements of Operations and Comprehensive Income, (ii) the Condensed Consolidated Balance Sheets, and (iii) the Condensed Consolidated Statements of Cash Flows, and (iv) Notes to Condensed Consolidated Financial Statements, tagged as blocks of text
 - 101.INS XBRL Instance Document
 - 101.SCH XBRL Taxonomy Extension Schema Document
 - 101.CAL XBRL Taxonomy Extension Calculation Linkbase Document

Table of Contents

101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document

29

Table of Contents

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.

Plexus Corp.
Registrant

2/4/11
Date /s/ Dean A. Foate
Dean A. Foate
President and Chief Executive Officer

2/4/11
Date /s/ Ginger M. Jones
Ginger M. Jones
Vice President and Chief Financial Officer