SMTC CORP
Form 10-Q
November 12, 2010
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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 October 3, 2010

OR

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

FOR THE TRANSITION PERIOD FROM TO

COMMISSION FILE NUMBER 0-31051

SMTC CORPORATION

(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

DELAWARE	**98-0197680**
(STATE OR OTHER JURISDICTION OF	**(I.R.S. EMPLOYER**
INCORPORATION OR ORGANIZATION)	**IDENTIFICATION NO.)**

635 HOOD ROAD

MARKHAM, ONTARIO, CANADA L3R 4N6

(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES) (ZIP CODE)

(905) 479-1810

(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 x 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 ¨ 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: definition of accelerated filer, large accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large Accelerated Filer	¨	Accelerated Filer	¨
Non-accelerated Filer	¨	Smaller reporting company	x

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

As of October 31, 2010, SMTC Corporation had 15,067,487 shares of common stock, par value $0.01 per share, and one share of special voting stock, par value $0.01 per share, outstanding. As of October 31, 2010, SMTC Corporation s subsidiary, SMTC Manufacturing Corporation of Canada, had 583,848 exchangeable shares outstanding, excluding 7,364,462 exchangeable shares owned by the Company s wholly-owned subsidiary, SMTC Nova Scotia Company, each of which is exchangeable for one share of common stock of SMTC Corporation.

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SMTC CORPORATION

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Part I FINANCIAL INFORMATION

Item 1 Financial Statements

Consolidated Balance Sheets as of:

(Expressed in thousands of U.S. dollars)

(Unaudited)

	October 3, 2010	January 3, 2010
Assets		
Current assets:		
Cash	$ 2,108	$ 1,589
Accounts receivable net (note 3)	35,868	37,688
Inventories (note 3)	45,069	37,026
Prepaid expenses	1,464	2,122
	84,509	78,425
Property, plant and equipment net (note 3)	13,353	14,266
Deferred financing costs net (note 3)	535	627
Deferred income taxes (note 7)	300	290
	$ 98,697	$ 93,608
Liabilities and Shareholders Equity		
Current liabilities:		
Accounts payable	$ 41,522	$ 41,589
Accrued liabilities (note 3)	8,317	6,218
Income taxes payable	554	540
Current portion of long-term debt (note 4)	2,904	5,013
Current portion of capital lease obligations	870	789
	54,167	54,149
Long-term debt (note 4)	17,211	20,666
Capital lease obligations	303	543
Commitments and contingencies (note 11)		
Shareholders equity:		
Capital stock (note 5)	6,046	7,093
Additional paid-in capital	255,292	253,304
Deficit	(234,322)	(242,147)
	27,016	18,250
	$ 98,697	$ 93,608

See accompanying notes to consolidated financial statements.

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Consolidated Statements of Operations and Comprehensive Income (Loss)

(Expressed in thousands of U.S. dollars, except number of shares and per share amounts)

(Unaudited)

		Three months ended		Nine months ended	
		October 3, 2010	October 4, 2009	October 3, 2010	October 4, 2009
Revenue		$ 65,381	$ 44,181	$ 197,950	$ 128,272
Cost of sales		57,518	40,446	175,360	116,622
Gross profit		7,863	3,735	22,590	11,650
Selling, general and administrative expenses		4,737	2,760	13,115	9,362
Restructuring charges	Note 6				783
Operating earnings		3,126	975	9,475	1,505
Interest expense	Note 3	436	473	1,376	1,338
Earnings before income taxes		2,690	502	8,099	167
Income tax expense	Note 7				
Current		118	23	284	67
Deferred		(9)	17	(10)	129
		109	40	274	196
Net earnings (loss) from continuing operations		2,581	462	7,825	(29)
Loss from discontinued operations	Note 10		(297)		(5,744)
Net earnings (loss), also being comprehensive income (loss)		$ 2,581	$ 165	$ 7,825	$ (5,773)
Earnings (loss) per share of common stock:					
Basic					
Continuing operations		$ 0.17	$ 0.03	$ 0.53	$
Discontinued operations			(0.02)		(0.39)
Total		$ 0.17	$ 0.01	$ 0.53	$ (0.39)
Diluted					
Continuing operations		$ 0.16	$ 0.03	$ 0.51	$
Discontinued operations			(0.02)		(0.39)
Total		$ 0.16	$ 0.01	$ 0.51	$ (0.39)
Weighted average number of shares outstanding					
Basic		15,049,668	14,646,333	14,841,673	14,646,333
Diluted	Note 8	15,745,506	14,646,333	15,422,228	14,646,333

See accompanying notes to consolidated financial statements.

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Consolidated Statements of Changes in Shareholders Equity

(Expressed in thousands of U.S. dollars)

Nine months ended October 3, 2010 and October 4, 2009

(Unaudited)

	Capital stock	Warrants	Additional paid-in capital	Deficit	Shareholders equity
Balance, January 3, 2010	$ 7,093	$	$ 253,304	$ (242,147)	$ 18,250
Stock-based compensation			139		139
Conversion of shares from exchangeable to common stock	(1,052)		1,052		
Exercise of stock options	5		797		802
Net income				7,825	7,825
Balance, October 3, 2010	$ 6,046	$	$ 255,292	$ (234,322)	$ 27,016

	Capital stock	Warrants	Additional paid-in capital	Deficit	Total Shareholders equity
Balance, January 4, 2009	$ 7,456	$ 10,372	$ 249,655	$ (246,169)	$ 21,314
Cumulative effect of change in accounting principle January 5, 2009 reclassification of warrants to opening deficit		(7,617)		7,617	
Adjusted balance, January 5, 2009	$ 7,456	$ 2,755	$ 249,655	$ (238,552)	$ 21,314
Stock-based compensation			217		217
Conversion of shares from exchangeable to common stock	(245)		245		
Expiry of warrants		(2,755)	2,755		
Net loss				(5,773)	(5,773)
Balance, October 4, 2009	$ 7,211	$	$ 252,872	$ (244,325)	$ 15,758

See accompanying notes to consolidated financial statements.

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Consolidated Statements of Cash Flows

(Expressed in thousands of U.S. dollars)

(Unaudited)

	Three months ended		Nine months ended	
	October 3, 2010	October 4, 2009	October 3, 2010	October 4, 2009
Cash provided by (used in):				
Operations:				
Net income (loss)	$ 2,581	$ 165	$ 7,825	$ (5,773)
Items not involving cash:				
Depreciation	643	695	1,892	2,093
Gain on disposition of property, plant and equipment				(224)
Deferred income taxes	(9)	17	(10)	129
Non-cash interest	55	64	192	192
Stock-based compensation	217	68	865	256
Change in non-cash operating working capital:				
Accounts receivable	8,400	(3,987)	1,820	(1,485)
Inventories	1,404	173	(8,043)	9,510
Prepaid expenses	182	(384)	658	(255)
Income taxes payable	36	61	14	74
Accounts payable	(9,612)	1,322	(67)	(7,499)
Accrued liabilities	698	(675)	1,400	(276)
	4,595	(2,481)	6,546	(3,258)
Financing:				
Increase (decrease) in revolving debt	(4,703)	3,117	(5,339)	3,925
Repayment of long-term debt	(75)	(563)	(225)	(1,363)
Principal payment of capital lease obligations	(211)	(207)	(594)	(1,186)
Proceeds from sale and leaseback	435		435	
Deferred financing costs			(100)	(151)
Proceeds from issuance of common stock	134		802	
	(4,420)	2,347	(5,021)	1,225
Investing:				
Purchase of property, plant and equipment	(170)	(702)	(1,006)	(984)
Proceeds from sale of property, plant and equipment				830
	(170)	(702)	(1,006)	(154)
Increase (decrease) in cash	5	(836)	519	(2,187)
Cash, beginning of period	2,103	1,272	1,589	2,623
Cash, end of the period	$ 2,108	$ 436	$ 2,108	$ 436

See accompanying notes to consolidated financial statements.

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Notes to Consolidated Financial Statements

1. Nature of the business

SMTC Corporation (the Company) is a worldwide provider of advanced electronics manufacturing services to original equipment manufacturers. The Company services its customers through manufacturing and technology centers located in the United States, Canada, Mexico and China. For the past nine years the Company has had an evolving manufacturing relationship with Alco Electronics Ltd. (Alco), a Hong Kong headquartered, publicly-traded company with large scale manufacturing operations in China. The Company operates under a manufacturing agreement with Alco, having established a dedicated manufacturing facility in Chang An, China. Capitalizing on the strengths of both companies, this site provides the Company s current and prospective customers with highly efficient, low cost Asia-based manufacturing solutions. The facility provides a full suite of integrated manufacturing services including assembly, testing, box build, final product integration, and expanded supply chain capabilities through an international sourcing and procurement office.

Effective June 30, 2009, the Company closed its Boston, Massachusetts facility. Results of this operation are reported as discontinued operations for the comparative reporting periods.

The unaudited interim consolidated financial statements of the Company have been prepared in accordance with the accounting principles and methods of application disclosed in the audited consolidated financial statements within the Company s Form 10-K for the fiscal period ended January 3, 2010, (Form 10-K) filed with the Securities and Exchange Commission (the SEC) on March 19, 2010, except as described in Note 2. The accompanying unaudited interim consolidated financial statements include adjustments that are, in the opinion of management, necessary for a fair presentation under generally accepted accounting principles in the United States (U.S. GAAP). These unaudited interim consolidated financial statements should be read in conjunction with the Company s audited consolidated financial statements for the period ended January 3, 2010.

2. Recent accounting pronouncements and changes in accounting estimates

Recent Accounting Pronouncements

In September 2009, the FASB issued ASU No. 2009-13, Multiple-Deliverable Revenue Arrangements a consensus of the FASB Emerging Issues Task Force (ASU 2009-13). It updates the existing multiple-element revenue arrangements guidance currently included under ASC 605, Revenue Recognition . The revised guidance primarily provides two significant changes: 1) eliminates the need for objective and reliable evidence of the fair value for the undelivered element in order for a delivered item to be treated as a separate unit of accounting, and 2) eliminates the residual method to allocate the arrangement consideration. In addition, the guidance also expands the disclosure requirements for revenue recognition. ASU 2009-13 will be effective for the first annual reporting period beginning on or after June 15, 2010, with early adoption permitted provided that the revised guidance is retroactively applied to the beginning of the year of adoption. The Company is currently assessing the future impact of this ASU to its consolidated financial statements.

Changes in Accounting Estimates

In the course of acquiring machinery and equipment used in the surface mount process at the beginning of the first quarter of 2010, the Company conducted an asset by asset review of the estimated useful lives of machinery and equipment used in that process. Based on those findings, the estimated useful lives of certain items of that class of assets were increased from 7 years to approximately 10 years. This change in estimate was applied to all existing and new assets of this class on a prospective basis from January 3, 2010. This change in estimate for the quarter ended October 3, 2010 resulted in an increase to net income of $71 and no change to earnings per share, and for the nine months ended October 3, 2010, an increase to net income of $213 and a $0.01 increase to earnings per share.

3. Consolidated financial statement details

The following consolidated financial statement details are presented as of the period ended for the consolidated balance sheets and for the three and nine months ended for each of the consolidated statements of operations and comprehensive income (loss) and consolidated statements of cash flows.

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Notes to Consolidated Financial Statements (Continued)

Consolidated balance sheets

Accounts receivable net:

	October 3, 2010	January 3, 2010
Accounts receivable	$ 35,643	$ 37,709
Taxes receivable	537	537
Allowance for doubtful accounts	(312)	(558)
Accounts receivable net	$ 35,868	$ 37,688

Inventories:

	October 3, 2010	January 3, 2010
Raw materials	$ 31,038	$ 22,618
Work in process	10,077	10,564
Finished goods	2,827	2,789
Parts	1,127	1,055
Inventories	$ 45,069	$ 37,026

Deferred financing costs:

	October 3, 2010	January 3, 2010
Deferred financing costs	$ 2,777	$ 2,677
Accumulated amortization	(2,242)	(2,050)
	$ 535	$ 627

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Notes to Consolidated Financial Statements (Continued)

Property, plant and equipment net:

	October 3, 2010	January 3, 2010
Cost:		
Land	$ 1,648	$ 1,648
Buildings	9,873	9,852
Machinery and equipment (a)	30,900	30,065
Office furniture and equipment	2,393	2,393
Computer hardware and software (b)	9,088	8,959
Leasehold improvements	3,120	3,099
	57,022	56,016
Less accumulated depreciation:		
Land		
Buildings	(5,154)	(4,776)
Machinery and equipment (a)	(24,493)	(23,186)
Office furniture and equipment	(2,321)	(2,305)
Computer hardware and software (b)	(8,769)	(8,592)
Leasehold improvements	(2,932)	(2,891)
	(43,669)	(41,750)
Property, plant and equipment net	$ 13,353	$ 14,266

(a) Included within machinery and equipment were assets under capital leases with costs of $7,576 and $7,141 as at October 3, 2010 and January 3, 2010, respectively and associated accumulated depreciation of $4,709 and $3,998 as of October 3, 2010 and January 3, 2010, respectively. The related depreciation expense for the three months ended October 3, 2010 and October 4, 2009 were $280 and $248, respectively. Related depreciation expense for the nine months ended October 3, 2010 and October 4, 2009 was $711 and $766, respectively.

(b) Included within computer hardware and software were assets under capital leases with costs of $268 as at both October 3, 2010 and January 3, 2010, and associated accumulated depreciation of $203 and $137, as of October 3, 2010 and January 3, 2010, respectively. The related depreciation expense for both the three months ended October 3, 2010 and October 4, 2009 was $22. Related depreciation expense for both the nine months ended October 3, 2010 and October 4, 2009 was $66.

Accrued liabilities:

	October 3, 2010	January 3, 2010
Customer related	$ 1,794	$ 1,277
Payroll	5,037	2,079
Professional services	601	488

Restructuring and discontinued operations	42	884
Vendor related	124	498
Miscellaneous taxes	159	228
Other	560	764
Accrued liabilities	$ 8,317	$ 6,218

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Notes to Consolidated Financial Statements (Continued)

Consolidated statements of operations

Interest expense:

	Three months ended		Nine months ended	
	October 3, 2010	**October 4, 2009**	**October 3, 2010**	**October 4, 2009**
Long-term debt	$ 399	$ 439	$ 1,382	$ 1,191
Obligations under capital leases	35	32	97	160
Other	2	2	(103)	(13)
Interest expense	$ 436	$ 473	$ 1,376	$ 1,338

Consolidated statements of cash flows

Supplemental disclosures:

	Three months ended		Nine months ended	
	October 3, 2010	**October 4, 2009**	**October 3, 2010**	**October 4, 2009**
Cash interest paid	$ 390	$ 423	$ 1,302	$ 1,381
Cash taxes paid net	$ 79	$ 19	$ 256	$ 67

4. Long-term debt

	October 3, 2010	**January 3, 2010**
Revolving	$ 10,727	$ 16,066
Term	9,388	9,613
	20,115	25,679
Less: Current portion of long-term debt	(2,904)	(5,013)
Long-term debt	$ 17,211	$ 20,666

The Company has a loan agreement with Wells Fargo Capital Finance Corporation Canada (Wells Fargo) (formerly Wachovia Capital Finance Corporation (Canada)) and Export Development Canada (EDC), to be referred to collectively as the Wells Fargo EDC Facilities .

On April 2, 2009, the Company received a waiver from its lenders. The Company and its lenders amended the lending agreements to revise the EBITDA and leverage covenants and eliminate the fixed charge coverage ratio for the five quarters beginning January 5, 2009 and including the first quarter of the 2010 fiscal period. The interest rate was increased by 200 to 300 basis points. On August 4, 2009, a further amendment was obtained, effectively extending the terms of the April agreement to July 2010. On May 18, 2010, the Company and its lenders signed an amendment to extend the repayment schedule and the term of the debt agreement to August 2013, to reset the EBITDA and leverage covenants,

to eliminate the fixed charge coverage ratio covenant, and to reduce interest rates. The revolving line of credit now bears interest at prime to prime plus 1%, the term loan to EDC now bears interest at LIBOR plus 2.5% to 3.5 %, and the term loan to Wells Fargo now bears interest at LIBOR plus 3% to 4%, depending on the achievement of financial performance levels as specified in the debt agreement.

The Company incurred costs of $100 related to the amendment of the Wells Fargo EDC Facilities in 2010, and $151 in 2009. These costs were recorded as a non-current deferred charge and are being amortized as additional interest expense over the remaining term of the credit facility.

Under the new amendment, repayments of the term loan to EDC for fiscal 2010 have been postponed. Payments are scheduled to recommence on April 1, 2011 with quarterly installments of $926, and the remaining amounts outstanding due at maturity. The term loan to Wells Fargo is repayable in quarterly installments of $75, with the remaining amounts outstanding due at maturity.

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Notes to Consolidated Financial Statements (Continued)

The Wells Fargo EDC Facilities are jointly and severally guaranteed by the Company and secured by the assets and capital stock of each of the Company s subsidiaries and its future subsidiaries.

At October 3, 2010 and January 3, 2010, there were Canadian dollar denominated cash balances of $6,958 and $6,997 respectively, which were classified as offsets to debt balances as they were used to reduce the outstanding revolving credit facilities.

The Company is in compliance with the financial covenants included in the amended Wells Fargo EDC Facilities as at October 3, 2010. Management believes that the Company will be in compliance with these covenants for the foreseeable future. Accordingly, the outstanding balances under the lending agreements continue to be classified as long-term. Continued compliance with its covenants, however, is dependent on the Company achieving certain forecasts. While management is confident in its plans, there is no assurance that the Company will achieve its forecasts. In the event of non-compliance, the Company s lenders have the right to demand repayment of the amounts outstanding under the lending agreements or pursue other remedies or, if the Company can reach an agreement with its lenders, to amend or waive the financial covenants.

5. Capital stock

Common shares

Issued and outstanding:

The issued and outstanding number of common shares included in shareholders equity consisted of the following as of October 3, 2010:

	Number of shares	$
Common Stock		
Exchangeable shares:		
Balance at beginning of the nine month period	711,048	$ 6,728
Shares issued pursuant to:		
Conversion to common stock	(111,200)	(1,053)
Balance at end of the period	599,848	$ 5,675
Common shares:		
Balance at beginning of the nine month period	13,935,284	$ 365
Shares issued pursuant to:		
Exercise of stock options	502,088	5
Conversion of exchangeable shares	111,200	1
Balance at end of the period	14,548,572	$ 371
Special voting stock:		
Balance at beginning of the nine month period	1	$
Balance at end of the period	1	$
Total Common stock	15,148,421	$ 6,046

Warrants

Common Share Warrants:

On June 1, 2004, the Company s pre-existing lenders exchanged $10,000 of outstanding debt and all warrants previously issued or required to be issued for 2,233,389 shares of common stock and 11,166,947 warrants (the Conversion Warrants). Each warrant was exercisable for one-tenth of one share of common stock of the Company at an exercise price of $6.90 per share of common stock. The Conversion Warrants expired on March 4, 2009. Upon expiry of the unexercised warrants, the amount attributed to the Conversion Warrants was recorded as additional paid-in capital.

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Notes to Consolidated Financial Statements (Continued)

Exchangeable Share Warrants:

On March 3, 2004, the Company completed a private placement of 33,350,000 Special Warrants (each Special Warrant and collectively, the Special Warrants) of SMTC Manufacturing Corporation of Canada (SMTC Canada), an indirect subsidiary of the Company. Each Special Warrant was issued at a price of CDN $1.20 per Special Warrant.

Subject to the satisfaction of applicable legal requirements, each Special Warrant was exercisable for one unit, consisting of one-fifth of an exchangeable share of SMTC Canada, and one-half of a warrant to purchase one-fifth of an exchangeable share of SMTC Canada. Each whole warrant (a Purchase Warrant) was exercisable for one-fifth of an exchangeable share of SMTC Canada at an exercise price of CDN $9.25 per share. The Special Warrants were exercised into units on June 2, 2004. The Purchase Warrants expired unexercised on March 3, 2009.

Upon the adoption of guidance under ASC 815, Derivatives and Hedging , on determining whether an instrument (or embedded feature) is indexed to an entity s own stock on January 5, 2009, the Purchase Warrants were retrospectively reclassified as liabilities, without restatement of prior periods, as disclosed in Note 2 of the Form 10-K. As the fair value of these instruments at that date was determined to be nil, the amount attributed to these warrants was recorded as a reduction of opening deficit on January 5, 2009.

Stock options

For information regarding the Company s stock option arrangements, see Note 6 of Form 10-K. There were no options granted during the three and nine month periods ended October 3, 2010. The Company generally issues new shares when options are exercised. A summary of stock option activity for the nine month period ended October 3, 2010 is as follows:

	Number of options	Weighted average exercise price	Aggregate intrinsic value	Weighted average remaining contractual term (years)
Outstanding at January 3, 2010	1,937,440	$ 1.72		
Options forfeited	(3,767)	$ 6.48		
Options exercised	(502,088)	$ 1.64		
Outstanding at October 3, 2010	1,431,585	$ 1.74	$ 2,934	3.3
Exercisable at October 3, 2010	756,589	$ 2.39	$ 1,263	3.1

During the three month periods ended October 3, 2010 and October 4, 2009, the Company recorded stock-based compensation expense and a corresponding increase in contributed surplus of $42 and $68, respectively. For the nine month periods ended October 3, 2010 and October 4, 2009, the corresponding amounts recorded were $139 and $217, respectively. At October 3, 2010, compensation expense of $297 related to non-vested stock options had not been recognized.

Deferred share units

In previous periods, Deferred Share Units were granted to directors and the Chief Executive Officer of the Company as remuneration. No deferred share units were granted in the three and nine months ended October 3, 2010, or the three and nine months ended October 4, 2009.

As at October 3, 2010 and January 3, 2010, the Company had 249,113 and 335,666, respectively, deferred share units outstanding.

Deferred Share Unit compensation expense for the three and nine months ended October 3, 2010 was $175 and $726, respectively, compared with nil and $39 for the three and nine months ended October 4, 2009, reflecting mark-to-market adjustments.

There is no unrecognized compensation related to deferred share units since these awards vest immediately when granted.

6. Restructuring and other charges

In the first quarter of 2009, the Company recorded restructuring charges of $815, consisting of severance charges of $445 in the Mexican segment, $337 in the Canadian segment, and $33 in the U.S. segment. The Company reduced staff levels by approximately 160 in response to expected lower revenues resulting from the global economic recession. In the second quarter of 2009, the Company recorded a restructuring recovery of $32 consisting of a recovery on severances. There were no amounts in the restructuring accrual relating to the 2009 Plan as at either January 3, 2010 or October 3, 2010.

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Notes to Consolidated Financial Statements (Continued)

7. Income taxes

During the three and nine months ended October 3, 2010, the Company recorded a net income tax expense of $109 and $274, respectively, primarily related to minimum taxes in certain jurisdictions, combined with foreign exchange revaluation. During the three and nine months ended October 4, 2009, the Company recorded a net income tax expense of $40 and $196, respectively, primarily related to minimum taxes in certain jurisdictions, offset by foreign exchange revaluation.

At January 3, 2010, the Company had total net operating loss (NOL) carry forwards of $111,125, which will expire in the years presented below:

2010	$ 1,852
2012	1,260
2014	10,278
2015	4,154
2018	1,078
2019	60
2020	30
2021	19,160
2022	16,207
2023	27,270
2026-2029	29,776
	$ 111,125

At October 3, 2010 and January 3, 2010, the Company had gross unrecognized tax benefits of $308 and $312, respectively, which if recognized, would favorably impact the Company s effective tax rate in future periods. The change during the period relates to foreign exchange revaluation of existing uncertain tax positions. The Company does not expect any of these unrecognized tax benefits to reverse in the next twelve months.

Tax years 2002 to 2009 remain open for review by tax authorities in Canada. Tax years 2004 to 2009 remain open for review by tax authorities in the United States. In addition, 2001 contains an NOL that could potentially be carried forward and therefore remains open to the extent of the NOL.

The Company accounts for interest and penalties related to unrecognized tax benefits in income tax expense based on the likelihood of the event and its ability to reasonably estimate such amounts. The Company has approximately $197 and $203 accrued for interest and penalties as of October 3, 2010 and January 3, 2010, respectively. The change is primarily due to the recording of incremental interest on existing uncertain positions for the period and foreign exchange revaluation.

In assessing the realization of deferred tax assets, management considers whether it is more likely than not that some portion or all of its deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income. Management considers the scheduled reversal of deferred tax liabilities, change of control limitations, projected future taxable income and tax planning strategies in making this assessment. ASC 740, Income Taxes (ASC 740), states that forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence, such as cumulative losses in recent years in the jurisdictions to which the deferred tax assets relate. As a result of a review undertaken in the second quarter of 2003, the Company concluded that given the weakness and uncertainty in the economic environment at that time, it was appropriate to establish a full valuation allowance for the deferred tax assets arising from its operations in the jurisdictions to which the deferred tax assets relate. Commencing in 2004, it was determined by management that it was more likely than not that the deferred tax assets associated with the Mexican jurisdiction would be realized and no valuation allowance has been recorded against these deferred tax assets since 2004. The U.S. and Canadian jurisdictions continued to have a full valuation allowance established for the deferred tax assets. In addition, the Company expects to continue to provide a full valuation allowance for the assets relating

to the U.S and Canadian jurisdictions until it can demonstrate a sustained level of profitability that establishes its ability to utilize the assets in the jurisdictions to which the assets relate.

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Notes to Consolidated Financial Statements (Continued)

8. Earnings per common share

The following table details the weighted average number of common shares outstanding for the purposes of computing basic and diluted earnings per common share for the following periods:

	Three months ended		Nine months ended	
(Number of common shares)	**October 3, 2010**	**October 4 2009**	**October 3, 2010**	**October 4 2009**
Basic weighted average shares outstanding	15,049,668	14,646,333	14,841,673	14,646,333
Dilutive stock options [a] [b]	695,838		580,555	
Diluted weighted average shares outstanding	15,745,506	14,646,333	15,422,228	14,646,333

(a) As a result of the net loss from continuing operations for the nine months ended October 4, 2009, diluted earnings per share was calculated using the basic weighted average shares outstanding as the effect of potential common shares would have been anti-dilutive.

(b) For the three months ended October 3, 2010 and October 4, 2009, as a result of net earnings from continuing operations, dilutive options were determined using the treasury stock method, using an average share price of $3.02 and $0.78 per share, respectively. For the three months ended October 3, 2010 and October 4, 2009, the calculation did not include 93,673 and 1,267,440 stock options, respectively, as the effect would have been anti-dilutive. For the nine months ended October 3, 2010, dilutive options were determined using the treasury stock method, using an average share price of $2.68 per share. The calculation did not include 290,340 stock options as the effect would have been anti-dilutive.

9. Segmented information

General description

The Company derives its revenue from one dominant industry segment, the electronics manufacturing services industry. The Company is operated and managed geographically and has facilities in the United States, Canada, Mexico and Asia. Operations in Boston were classified as discontinued operations in the second quarter of 2009 and have been excluded from the United States segment in all periods presented. The Company monitors the performance of its geographic operating segments based on EBITA (earnings before interest, taxes and amortization) and before restructuring charges and discontinued operations. Intersegment adjustments reflect intersegment sales that are generally recorded at prices that approximate arm s-length transactions. In assessing the performance of the operating segments management attributes revenue to the operating segment which ships the product. The Canadian segment absorbs a substantial portion of corporate costs. Information about the operating segments is as follows for the three and nine months ended October 3, 2010 and October 4, 2009:

	Three months ended		Nine months ended	
	October 3, 2010	**October 4, 2009**	**October 3, 2010**	**October 4, 2009**
Revenues from continuing operations				
Mexico	$ 32,417	$ 19,139	$ 93,657	$ 49,103
Asia	13,672	11,615	46,432	32,497
Canada	14,992	10,250	44,488	39,428
U.S.	5,519	3,862	17,369	9,823

Total	$ 66,600	$ 44,866	$ 201,946	$ 130,851
Intersegment revenue				
Mexico	$ (455)	$ (615)	$ (1,708)	$ (2,046)
Canada	(762)	(67)	(2,223)	(524)
U.S.	(2)	(3)	(65)	(9)
Total	$ (1,219)	$ (685)	$ (3,996)	$ (2,579)
Net external revenue from continuing operations				
Mexico	$ 31,962	$ 18,524	$ 91,949	$ 47,058
Asia	13,672	11,615	46,432	32,497
Canada	14,230	10,183	42,265	38,904
U.S.	5,517	3,859	17,304	9,814
Total	$ 65,381	$ 44,181	$ 197,950	$ 128,272
EBITA				
Mexico	$ 4,185	$ 1,233	$ 11,729	$ 3,040
Asia	430	324	1,264	903
Canada	(2,059)	(562)	(5,369)	(1,067)
U.S.	570	(20)	1,851	(588)
Total	$ 3,126	$ 975	$ 9,475	$ 2,288
Interest	436	473	1,376	1,338
Restructuring charges				783
Earnings before income taxes	$ 2,690	$ 502	$ 8,099	$ 167

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Notes to Consolidated Financial Statements (Continued)

Capital additions

The following table contains capital additions for the three and nine months ended October 3, 2010 and October 4, 2009:

	Three months ended		Nine months ended	
	October 3, 2010	October 4, 2009	October 3, 2010	October 4, 2009
Mexico	$ 64	$ 455	$ 195	$ 602
Asia	65	11	700	26
Canada	30	236	74	330
U.S.	11		37	26
Total	$ 170	$ 702	$ 1,006	$ 984

	October 3, 2010	January 3, 2010
Long-lived assets [(a)]		
Mexico	$ 10,207	$ 11,267
Asia	664	41
Canada	1,661	2,049
U.S.	821	909
Total	$ 13,353	$ 14,266

(a) Long-lived assets information is based on the principal location of the asset.

Geographic revenues

The following table contains geographic revenues based on the product shipment destination, for the three and nine months ended October 3, 2010 and October 4, 2009:

	Three months ended		Nine months ended	
	October 3, 2010	October 4, 2009	October 3, 2010	October 4, 2009
U.S.	$ 42,394	$ 21,846	$ 120,026	$ 51,513
Canada	16,857	15,911	49,063	55,856
Europe	5,870	99	15,700	457
Asia	257	6,319	13,149	20,429
Mexico	3	6	12	17
Total	$ 65,381	$ 44,181	$ 197,950	$ 128,272

Significant customers and concentration of credit risk:

Sales of the Company s products are concentrated in certain cases among specific customers in the same industry. The Company is subject to concentrations of credit risk in trade receivables. The Company considers concentrations of credit risk in establishing the allowance for doubtful accounts and believes the recorded allowances are adequate.

The Company expects to continue to depend upon a relatively small number of customers for a significant percentage of its revenue. In addition to having a limited number of customers, the Company manufactures a limited number of products for each customer. If the Company loses any of its larger customers or any product line manufactured for one of its larger customers, it could experience a significant reduction in revenue. Also, the insolvency of one or more of its larger customers or the inability of one or more of its larger customers to pay for its orders could decrease revenue. As many costs and operating expenses are relatively fixed, a reduction in net revenue can decrease profit margins and adversely affect the business, financial condition and results of operations.

During the three months ended October 3, 2010, three customers individually comprised 16.7%, 15.9% and 13.9% (October 4, 2009 four customers 23.8%, 16.8%, 13.9% and 13.5%) of total revenue from continuing operations across all geographic segments. During the nine months ended October 3, 2010 four customers individually comprised 16.5%, 14.9%, 13.4% and

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Notes to Consolidated Financial Statements (Continued)

13.4% (October 4, 2009 five customers 20.7%, 17.5%, 14.3%, 13.3% and 10.6%) of total revenue from continuing operations across all geographic segments. As of October 3, 2010, these customers represented 10%, 10%, 7% and 16%, respectively, (January 3, 2010, 35%, 24%, 3% and 9%, respectively) of the Company s trade accounts receivable.

10. Discontinued operations

In June 2009, the Company ceased manufacturing operations at its Boston, Massachusetts facility, which was formerly included in the United States reporting segment. The Company entered into an agreement with the landlord to terminate the existing lease and conducted a sale of plant equipment. As at July 5, 2009, the Boston facility was classified as a discontinued operation and its results of operations are separately reported for all periods presented. Summarized financial information for discontinued operations is presented below:

	Three months ended		Nine months ended	
	October 3, 2010	October 4, 2009	October 3, 2010	October 4, 2009
Discontinued Operations Before Disposal:				
Revenue	$	$ 638	$	$ 6,957
Loss from discontinued operations before disposal, net of taxes	$	$ (297)	$	$ (3,365)
Disposal:				
Loss on disposal, net of taxes				(2,379)
Loss from discontinued operations, net of taxes	$	$ (297)	$	$ (5,744)

The loss on disposal recorded in the nine months ended October 4, 2009 consist largely of the settlement under the lease termination agreement, severance costs and other contracted facility exit costs, somewhat offset by a gain on disposal of fixed assets.

The following is a summary of the loss on disposal recorded in the nine months ended October 4, 2009:

Severance	$ 742
Lease obligations	1,518
Other facility exit costs	343
Disposal of fixed assets	(224)
Total	$ 2,379

The following table details the change in the discontinued operations accrual for the three and nine months ended October 3, 2010:

	Severance	Lease Obligations	Other Facility Exit Costs	Total
Accruals related to discontinued operations	$ 742	$ 2,296	$ 343	$ 3,381
Cash payments	(517)	(1,709)	(271)	(2,497)
Accrual balance as at January 3, 2010	225	587	72	884

Cash payments	(78)	(430)	(20)	(528)
Accrual balance as at April 4, 2010	147	157	52	356
Cash payments	(84)	(157)	(20)	(261)
Accrual balance as at July 4, 2010	63		32	95
Cash payments	(51)		(2)	(53)
Accrual balance as at October 3, 2010	$ 12	$	$ 30	$ 42

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Notes to Consolidated Financial Statements (Continued)

11. Commitments and contingencies

In the normal course of business, the Company may be subject to litigation and claims from customers, suppliers and former employees. Management believes that adequate provisions have been recorded in the financial statements, as required. Although it is not possible to estimate the extent of potential costs, if any, management believes that ultimate resolution of such contingencies would not have a material adverse effect on the financial position, results of operations and cash flows of the Company.

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

Where we say we , us , our , the Company or SMTC , we mean SMTC Corporation or SMTC Corporation and its subsidiaries, as it may apply. Where we refer to the industry , we mean the electronics manufacturing services industry.

You should read this Management s Discussion and Analysis of Financial Condition and Results of Operations (MD&A) in combination with the accompanying unaudited interim consolidated financial statements and related notes as well as the audited consolidated financial statements and the accompanying notes to the consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP) included within the Company s Annual Report on Form 10-K filed on March 19, 2010. The forward-looking statements in this discussion regarding the electronics manufacturing services industry, our expectations regarding our future performance, liquidity and capital resources and other non-historical statements in this discussion include numerous risks and uncertainties, some of which are as described in the Risk Factors That May Affect Future Results section in the Annual Report on Form 10-K filed on March 19, 2010, as updated by Item 1A in Part II of this quarterly report. Certain statements in this MD&A contain words such as could , expects , may , anticipates , believes , intends , estimates , plans , envisions , seeks and other similar language and are considered forward looking statements or information under applicable securities laws. These statements are based on our current expectations, estimates, forecasts and projections about the operating environment, economies and markets in which we operate. These statements are subject to important assumptions, risks and uncertainties, which are difficult to predict and the actual outcome may be materially different. Although we believe expectations reflected in such forward-looking statements are reasonable based upon the assumptions in this MD&A, they may prove to be inaccurate and consequently our actual results could differ materially from our expectations set out in this MD&A. We may not update these forward-looking statements after the date of this Form 10-Q, even though our situation may change in the future. All forward-looking statements attributable to us are expressly qualified by these cautionary statements.

This MD&A contains discussion in U.S. dollars unless specifically stated otherwise.

Background

SMTC Corporation is a mid-tier provider of end-to-end electronics manufacturing services, or EMS, including product design and sustaining engineering services, printed circuit board assembly, or PCBA, production, enclosure fabrication, systems integration and comprehensive testing services. SMTC facilities span a broad footprint in the United States, Canada, Mexico and China, with approximately 1500 employees. SMTC s services extend over the entire electronic product life cycle from the development and introduction of new products through to growth, maturity and end-of-life phases. SMTC offers fully integrated contract manufacturing services with a distinctive approach to global original equipment manufacturers, or OEMs, and technology companies primarily within the industrial, computing and networking, and communications, consumer and medical market segments.

Developments in 2010

Third quarter results were significantly stronger than the same quarter last year as the Company s revenues increased by 48% and gross profit doubled compared with the third quarter of 2009. Several of the Company s longstanding customers continue to experience stronger end markets than those of 2009. Importantly, the Company has also experienced growth from several newer customers. Sequentially revenue decreased by 8% due largely to the substantial backlog in the first half of the year as customers rebuilt inventories in response to positive signs of an economic recovery.

For the quarter ended October 3, 2010, the Company recorded net income of $2.6 million compared to net income of $0.2 million in the prior year. The increase was mainly due to increased revenue and a higher gross profit percentage as a result of revenue mix and continued cost management. The Company generated $4.6 million in cash from operations which was largely used to pay down debt; net debt was reduced to $18.0 million which is consistent with our record low. The third quarter follows two strong quarters earlier in the year, including the second quarter which was a record quarter for the Company. For the second quarter of the year, the Company recorded net income of $3.2 million compared to a net loss of $3.4 million in the prior year. For the first quarter of the year, the Company recorded net income of $2.1 million.

On May 18, 2010, the Company and its lenders signed a favourable amendment to extend the repayment schedule and the term of the debt agreement to August 2013, to reset the EBITDA and leverage covenants, to eliminate the fixed charge coverage ratio covenant, and to reduce interest rates. The revolving line of credit now bears interest at prime to prime plus 1% and the term loan to EDC now bears interest at LIBOR plus 2.5% to 3.5%, depending on the achievement of financial performance levels as specified in the debt agreement. Under the new amendment, required repayments of the term loan to EDC for fiscal 2010 are eliminated. Payments are scheduled to recommence on April 1, 2011.

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Results of Operations

The consolidated financial statements of SMTC are prepared in accordance with U.S. GAAP.

Quarter ended October 3, 2010 compared with the quarter ended October 4, 2009:

The following table sets forth summarized operating results in millions of US$ for the periods indicated:

	Three months ended October 3, 2010		Three months ended October 4, 2009		Change 2010 to 2009	
	$	%	$	%	$	%
Revenue	$ 65.4	100.0%	$ 44.2	100.0%	$ 21.2	48.0%
Cost of sales	57.5	87.9%	40.4	91.4%	17.1	42.3%
Gross profit	7.9	12.1%	3.8	8.6%	4.1	107.9%
Selling, general and administrative expenses	4.8	7.3%	2.8	6.3%	2.0	71.4%
Operating earnings	3.1	4.7%	1.0	2.3%	2.1	210.0%
Interest expense	0.4	0.6%	0.5	1.1%	(0.1)	(20.0)%
Earnings from continuing operations before income taxes	2.7	4.1%	0.5	1.1%	2.2	451.0%
Income tax expense						
Current	0.1	0.2%		0.0%	0.1	
Deferred		0.0%		0.0%		
	0.1	0.2%		0.0%	0.1	
Income from continuing operations	2.6	4.0%	0.5	1.1%	2.1	430.6%
Loss from discontinued operations			(0.3)	(0.6)%	0.3	100.0%
Net earnings (loss)	$ 2.6	4.0%	$ 0.2	0.5%	$ 2.4	1268.4%

Revenue

Revenue from continuing operations increased $21.2 million, or 48.0%, from $44.2 million for the third quarter of 2009 to $65.4 million for the third quarter of 2010 as the majority of SMTC s long standing customers end markets continued to be favorably impacted by increased demand. In addition, newer customers, including those announced in the past several months, have contributed $9.4 million in increased revenue.

During the third quarter of 2010, revenue from the industrial sector increased compared with the same quarter of 2009; $53.1 million for the third quarter of 2010 compared with $37.3 million for the same period in 2009, as a result of increases for customers due to improved economic conditions. Revenue from the industrial sector as a percentage of total revenue decreased to 81.3% in the third quarter of 2010 compared with 84.6% in the third quarter of 2009.

Revenue from the communications sector increased compared with the same quarter of 2009; $4.3 million for the third quarter of 2010 compared with $1.0 million in 2009, which represented 6.6% of revenue in the third quarter of 2010, compared with 2.2% of revenue in the third quarter of 2009. The increase is due to two new customers ramping to production volumes as well as increased volumes from current customers.

Revenue from the networking and enterprise computing sector increased to $7.9 million for the third quarter of 2010 compared with $5.8 million in 2009, which represented 12.1% of revenue in the third quarter of 2010, down from 13.2% of revenue in the third quarter of 2009.

During the third quarter of 2010, the Company recorded approximately $1.3 million of sales of raw materials inventory to customers, which carried no margin, compared with $0.2 million in the third quarter of 2009. The Company purchases raw materials based on customer purchase orders. When a customer requires an order to be altered or changed, the customer is generally obligated to purchase the original on-order raw material at cost, to the extent the materials are not consumed within a specified period.

Due to changes in market conditions, the life cycle of products, the nature of specific programs and other factors, revenues from a particular customer typically varies from quarter to quarter and year to year. The Company s ten largest customers represented

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87.6% of revenue from continuing operations during the third quarter of 2010, compared with 95.0% in the third quarter of 2009. Revenue from our three largest customers during the third quarter of 2010 was $10.9 million, $10.4 million, and $9.1 million, representing 16.7%, 15.9%, and 13.9% of total revenue for the third quarter of 2010, respectively. This compares with revenue from our four largest customers of $10.5 million, $7.4 million, $6.1 million, and $5.9 million, representing 23.8%, 16.8%, 13.9%, and 13.5% of total revenue for the third quarter of 2009, respectively. No other customers represented more than 10% of revenue in either period.

During the third quarter of 2010, 48.9% of our revenue was attributable to production from our operations in Mexico, 21.8% in Canada, 20.9% in Asia and 8.4% in the U.S. During the third quarter of 2009, 41.9% of our revenue from continuing operations was attributable to our operations in Mexico, 23.1% in Canada, 26.3% in Asia, and 8.7% in the U.S.

The Company operates in a highly competitive and dynamic marketplace in which current and prospective customers from time to time seek to lower their costs through a competitive bidding process among EMS providers. This process creates an opportunity to increase revenue to the extent we are successful in the bidding process, however, there is also the potential for revenue to decline to the extent we are unsuccessful in this process. Furthermore, even if we are successful, there is potential for our margins to decline. If we lose any of our larger product lines manufactured for any one of our customers, we could experience declines in revenue.

Gross Profit

Gross profit for the third quarter of 2010 increased by $4.1 million, or 107.9%, to $7.9 million compared with the same period in 2009. This is largely due to increased revenue levels, leveraging fixed costs, combined with continued cost management. Gross margin as a percent of sales increased from 8.6% in the third quarter of 2009 to 12.1% in the third quarter of 2010 as a result of mix of revenue and cost management.

The Company adjusts for estimated obsolete or excess inventory for the difference between the cost of inventory and estimated realizable value based upon customer forecasts, shrinkage, the aging and future demand of the inventory, past experience with specific customers and the ability to sell back inventory to customers or suppliers. If these estimates change, additional write-downs may be required.

Selling, General & Administrative Expenses

Selling, general and administrative expenses increased by $2.0 million during the third quarter of 2010 to $4.8 million, from $2.8 million in the third quarter of 2009 largely as a result of accrued variable compensation, stock based compensation mark to market adjustments, increased staff, and higher professional fees.

Interest Expense

Interest expense decreased from $0.5 million in the third quarter of 2009 to $0.4 million for the third quarter of 2010, a decrease of $0.1 million primarily resulting from reduced debt levels and lower interest rates resulting from a favorable bank amendment. Interest expense in the third quarter of both 2010 and 2009 included amortization of deferred financing fees of $0.1 million. The weighted average interest rates with respect to the debt were 4.3% and 5.5% for each of the third quarters of 2010 and 2009, respectively.

Income Tax Expense

The Company recorded income tax expense of $0.1 million during the third quarter of 2010 compared to a nominal amount in the third quarter of 2009.

In assessing the realization of deferred tax assets, management considers whether it is more likely than not that some portion or all of its deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income. Management considers the scheduled reversal of deferred tax liabilities, change of control limitations, projected future taxable income and tax planning strategies in making this assessment. Guidance under ASC 740 states that forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence, such as cumulative losses in recent years in the jurisdictions to which the deferred tax assets relate. At the end of the second quarter of 2003, the Company concluded that given the weakness and uncertainty in the industry s economic environment at that time, it was appropriate to establish a full valuation allowance for the deferred tax assets. Commencing in 2004, it was determined by management that it was more likely than not that the deferred tax assets associated with the Mexican jurisdiction would be realized and no valuation allowance has been recorded against these deferred tax assets since 2004. The U.S. and Canadian jurisdictions continue to have a full valuation allowance recorded against the deferred tax assets in those jurisdictions.

At January 3, 2010, the Company had total net operating loss carry forwards of $111.1 million, of which $1.9 million will expire in 2010, $1.3 million will expire in 2012, $10.3 million will expire in 2014, $4.1 million will expire in 2015, $1.1 million will expire in 2018, $0.1 million will expire in 2019 and 2020, $19.2 million will expire in 2021, $16.2 million will expire in 2022, $27.3 million will expire in 2023, and the remainder will expire between 2026 and 2029.

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Discontinued Operations

In June 2009, the Company ceased manufacturing operations at its Boston, Massachusetts facility. The Company entered into an agreement with the landlord to terminate the existing lease and conducted a sale of certain plant equipment. As at July 5, 2009, the Boston facility was classified as a discontinued operation and its results of operations are separately reported for all periods presented.

Loss from discontinued operations before disposal was $0.3 million in the third quarter of 2009, and nil in the third quarter of 2010.

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Nine months ended October 3, 2010 compared with nine months ended October 4, 2009:

The following table sets forth summarized operating results in millions of US$ for the periods ended:

	Nine months ended October 3, 2010		Nine months ended October 4, 2009		Change 2010 to 2009	
	$	%	$	%	$	%
Revenue	$ 198.0	100.0%	$ 128.3	100.0%	$ 69.7	54.3%
Cost of sales	175.4	88.6%	116.6	90.9%	58.8	50.4%
Gross profit	22.6	11.4%	11.7	9.1%	10.9	93.2%
Selling, general and administrative expenses	13.1	6.6%	9.4	7.3%	3.7	39.4%
Restructuring charges		0.0%	0.8	0.6%	(0.8)	(100.0%)
Operating earnings	9.5	4.8%	1.5	1.2%	8.0	533.3%
Interest expense	1.4	0.7%	1.3	1.0%	0.1	7.7%
Income from continuing operations before income taxes	8.1	4.1%	0.2	0.2%	7.9	3950.0%
Income tax expense						
Current	0.3	0.2%	0.1	0.1%	0.2	200.0%
Deferred		0.0%	0.1	0.1%	(0.1)	(100.0%)
	0.3	0.2%	0.2	0.2%	0.1	50.0%
Income (loss) from continuing operations	7.8	3.9%		0.0%	7.8	
Loss from discontinued operations		0.0%	(5.8)	(4.4)%	5.8	100.0%
Net earnings (loss)	$ 7.8	3.9%	$ (5.8)	(4.4)%	$ 13.6	234.5%

Revenue

Revenue from continuing operations increased $69.7 million, or 54.3%, from $128.3 million for the first nine months of 2009 to $198.0 million for the first nine months of 2010 as many of SMTC s long standing customers end markets continued to be favorably impacted by increased demand and certain customers rebuilding inventory. In addition, newer customers, including those announced in the past several months, have contributed $26.6 million in increased revenue.

During the first nine months of 2010, revenue from the industrial sector represented 83.7% of revenue compared to 82.2% of revenue for the first nine months of 2009. Revenue generated from the industrial sector increased by $60.2 million to $165.6 million in the first nine months of 2010 compared to $105.4 million in the first nine months of 2009 for the reasons cited above.

In both relative and absolute terms, the revenue generated from the communications sector in the first nine months increased. During the first nine months of 2010, revenue from the communications sector represented 5.7% of revenue compared to 4.4% of revenue for the first nine months of 2009. In absolute terms, revenue increased by $5.6 million from $5.6 million in the first nine months of 2009 to $11.2 million in the first nine months of 2010 largely due to a new customer with $3.6 million of revenue and a $1.9 million increase from an existing customer.

Revenue from the networking and enterprise computing sector increased compared with the first nine months of 2009; $21.1 million or 10.6% of revenue for the first nine months of 2010 compared with $17.2 million or 13.4% of revenue in 2009. The increase is due to additional revenue from one long standing customer and revenue from a new customer.

During the first nine months of 2010, we recorded approximately $2.5 million of sales of raw materials inventory to customers, which carried no margin, compared to $1.0 million in the first nine months of 2009. The Company purchases raw materials based on customer purchase orders. To the extent the customer requires these orders to be altered or changed, the customer is generally obligated to purchase the original on-order raw material.

Due to changes in market conditions, the life cycle of products, the nature of specific programs and other factors, customer volumes produced by the Company typically vary from year to year. For the first nine months of 2010, the Company s ten largest customers represented 89.2% of revenue from continuing operations compared with 92.2% for the same period last year. Revenue

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from our four largest customers during the first nine months of 2010 was $32.7 million, $29.5 million, $26.5 million and $26.4 million, representing 16.5%, 14.9%, 13.4% and 13.4%, respectively, of total revenue for the period. This compares with revenues from five customers of $26.5 million, $22.5 million, $18.4 million, $17.0 million and $13.6 million, representing 20.7%, 17.5%, 14.3%, 13.3%, and 10.6%, respectively, of total revenue from continuing operations for the same period last year. No other customers represented more than 10% of revenue in either period.

During the first nine months of 2010, 46.5% of our revenue from continuing operations was produced from operations in Mexico, 23.5% from Asia, 21.4% from Canada and 8.6% from the United States. During the first nine months of 2009, 36.7% of our revenue from continuing operations was produced from operations in Mexico, 25.3% from Asia, 30.3% from Canada and 7.7% from the United States. The variance in Mexico and Canada is due to production of three customers being moved to Mexico from Canada.

The Company operates in a highly competitive and dynamic marketplace in which current and prospective customers from time to time seek to lower their costs through a competitive tendering process among EMS providers. This process creates an opportunity to increase revenue to the extent we are successful in the tender process; however there is also the potential for revenue to decline to the extent we are unsuccessful in this process. Furthermore, even if we are successful, there is potential for our margins to decline. If we lose any of the larger product lines manufactured for any one of our customers, we could experience declines in revenue.

Gross Profit

Gross profit increased $10.9 million from $11.7 million, or 9.1% of revenue, for the first nine months of 2009 to $22.6 million, or 11.4% of revenue, for the first nine months of 2010. The increase in the gross margin in the first nine months of 2010 is largely due to increased revenue leveraging fixed costs combined with improved efficiency as a result of cost containment initiatives and a change in revenue mix.

The Company adjusts for estimated obsolete or excess inventory for the difference between the cost of inventory and estimated realizable value based upon customer forecasts, shrinkage, the aging and future demand of the inventory, past experience with specific customers and the ability to sell back inventory to customers or suppliers. If these estimates change, additional write-downs may be required.

Selling, General & Administrative Expenses

Selling, general and administrative expenses increased in absolute dollars but decreased as a percent of sales. Selling, general and administrative expenses increased $3.7 million from $9.4 million, or 7.3% of revenue, for the first nine months of 2009 to $13.1 million, or 6.6% of revenue, for the first nine months of 2010. The increase in absolute dollars in 2010 is largely related to higher accrued variable compensation, stock based compensation mark to market adjustments, salary expense, legal and other professional fees.

Restructuring Charges

In the first nine months of 2009 the Company recorded restructuring charges of $0.8 million, consisting of severance charges of $0.5 million in the Mexican segment, $0.3 million in the Canadian segment and a nominal amount in the U.S. segment. The Company reduced staff levels by approximately 160 in response to expected lower revenues resulting from the global economic recession. No restructuring charges occurred in the first nine months of 2010.

Interest Expense

Interest expense increased $0.1 million from $1.3 million for the first nine months of 2009 to $1.4 million for the first nine months of 2010, resulting from increased debt levels in the first half of 2010, somewhat offset by a reduction in the interest rate. Interest expense for the first nine months of both 2010 and 2009 include amortization of deferred financing fees of $0.2 million. The weighted average interest rates with respect to the debt for the first nine months of 2010 and 2009 were 5.0% and 5.3%, respectively.

Income Tax Expense

The Company recorded net income tax expense of $0.3 million during the first nine months of 2010, compared to $0.2 million during the first nine months of 2009, relating to minimum taxes in certain jurisdictions, combined with foreign exchange revaluation.

Discontinued Operations

Loss from discontinued operations before disposal was $3.4 million in the first nine months of 2009, and nil in the first nine months of 2010.

The $2.4 million loss on disposal recorded in the nine months ended October 4, 2009 consist largely of the settlement under the lease termination agreement, severance costs and other contracted facility exit costs, somewhat offset by a gain on disposal of fixed assets at the former Boston facility.

Liquidity

Net cash provided in operating activities during the nine months ended October 3, 2010 was $6.5 million driven by the net income generated by the Company. Net working capital increased by $4.2 million due to increases in inventory, which was partially offset by decreases in accounts receivable and increases in accrued liabilities. Accounts receivable days sales outstanding were 49 and 64 days for the nine months ended October 3, 2010 and October 4, 2009, respectively. Inventory turnover, on an annualized basis was 5.2 times for the nine months ended October 3, 2010 and compared to 5.7 times for the nine months ended October 4, 2009. Accounts payable days outstanding were 65 days at the end of the first nine months of 2010 compared to 70 days for the same period in 2009.

Net cash used in financing activities during the nine months ended October 3, 2010 was $5.0 million and net cash provided in the nine months ended October 4, 2009 was $1.2 million. During the nine months ended October 3, 2010, the Company repaid debt of $5.6 million, while during the same period in 2009 the Company s net debt increased $2.6 million. During the nine months ended October 3, 2010 the Company generated $0.8 million in proceeds from the issuance of common stock upon the exercise of stock options. During the nine months ended October 3, 2010 the Company received proceeds of $0.4 million from the sales and leaseback of fixed assets. Cash used in financing activities during the nine months ended October 4, 2009 included a $1.2 million repayment of capital lease obligations as a result of the disposition of property, plant and equipment in Boston.

Net cash used in investing activities during the nine months ended October 3, 2010 was $1.0 million, consisting of additions of property, plant and equipment. Net cash used in the nine months ended October 4, 2009 was $0.2 million, consisting of additions of property, plant and equipment of $1.0 million, partially offset by $0.8 million provided by proceeds on the disposition of property, plant and equipment in Boston.

All accruals related to the disposal of the Boston facility are expected to be settled by the end of the fourth quarter of 2010.

Capital Resources

On May 18, 2010, the Company and its lenders signed an amendment to extend the repayment schedule and the term of the debt agreement to August 2013, to reset the EBITDA and leverage covenants, to eliminate the fixed charge coverage ratio covenant, and to reduce interest rates. The revolving line of credit now bears interest at prime to prime plus 1%, the term loan to EDC now bears interest at LIBOR plus 2.5% to 3.5%, and the term loan to Wells Fargo now bears interest at LIBOR plus 3% to 4%, depending on the achievement of financial performance levels as specified in the debt agreement. Under the new amendment, required repayments of the term loan to EDC for fiscal 2010 are eliminated. Payments are scheduled to recommence on April 1, 2011.

We believe that cash generated from operations, available cash and amounts available under our Wells Fargo EDC Facilities and additional financing sources such as leasing companies and other lenders will be adequate to meet our debt service requirements, capital expenditures and working capital needs at our current level of operations and organic growth in the future, although no assurance can be given in this regard, particularly with respect to amounts available from lenders. We have agreed to a borrowing base formula under which the amount we are permitted to borrow under the Wells Fargo EDC Facilities is based on our accounts receivable and inventory. Further, there can be no assurance that our business will generate sufficient cash flow from operations or that future borrowings will be available to enable us to service our indebtedness. Our future operating performance and ability to service indebtedness will be subject to future economic conditions and to financial, business and other factors, certain of which are beyond our control.

During the nine months ended October 3, 2010, the Company sold and leased back machinery and equipment for $0.4 million as a financing transaction. The assets are classified on the balance sheet as machinery and equipment under capital lease.

Item 3 Quantitative and Qualitative Disclosures about Market Risk

Interest Rate Risk

Our credit facilities bear interest at floating rates. The weighted average interest rate incurred on debt for the quarter ended October 3, 2010 was 4.3%. At October 3, 2010, the interest rate on our U.S. revolving credit facility is 4.25% based on the U.S. prime rate, our U.S. term debt bore interest at 3.76% based on LIBOR and our Canadian term debt bore interest at 4.25% based on LIBOR. If base rates increased by 10%, our interest expense would have increased by approximately $0.1 million annually.

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Foreign Currency Exchange Risk

Most of our sales and component purchases are denominated in U.S. dollars. Our Canadian and Mexican payroll, Euro based component purchases and other various expenses are denominated in local currencies. As a result, we have limited exposure to foreign currency exchange risk for modest changes in exchange rates. However, for more significant changes in exchange rates, the Company is subject to much greater variations. Every $0.01 change in the US dollar results in a change in expenses of approximately $0.2 million. The strengthening of the Canadian dollar and the Mexican peso results in an increase in costs to the organization and may lead to a reduction in reported earnings.

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Item 4T Controls and Procedures

Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this quarterly report, the Company s Principal Executive Officer and Principal Financial Officer have conducted an evaluation of the Company s disclosure controls and procedures. Based on their evaluation, the Company s Principal Executive Officer and Principal Financial Officer have concluded that the Company s disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Securities Exchange Act of 1934 is (i) recorded, processed, summarized and reported within the time periods specified in the applicable Securities and Exchange Commission rules and forms and (ii) accumulated and communicated to the Company s management, including the Company s Principal Executive Officer and the Company s Principal Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Controls and Procedures

There was no change in the Company s internal controls over financial reporting or in other factors that has materially affected, or is reasonably likely to materially affect these controls identified in connection with the most recent evaluation of these controls by the Company s Principal Executive Officer and Principal Financial Officer.

Part II OTHER INFORMATION

Item 1A Risk Factors

Other than with respect to the risk factors below, there have been no material changes from the risk factors disclosed in the Risk Factors section of the Company s Annual Report on Form 10-K for the period ended January 3, 2010. The three risk factors below were disclosed on the Form 10-K and have been updated to provide revised information as of October 3, 2010.

A majority of our revenue comes from a small number of customers; if we lose any of our larger customers, our revenue could decline significantly.

We operate in a highly competitive and dynamic marketplace in which current and prospective customers often seek to lower their costs through a competitive bidding process among EMS providers. This process creates an opportunity to increase revenue to the extent we are successful in the bidding process, however, there is also the potential for revenue decline to the extent we are unsuccessful in the process. Furthermore, even if we are successful, there is the potential for our margins to decrease.

Our four largest customers represented 16.5%, 14.9%, 13.4% and 13.4% of total revenue from continuing operations for the nine months ended October 3, 2010, respectively. For the first nine months of 2010, our top ten largest customers collectively represented 89.2% of our total revenue. We expect to continue to depend upon a relatively small number of customers for a significant percentage of our revenue. In addition to having a limited number of customers, we manufacture a limited number of products for each of our customers. If we lose any of our largest customers or any product line manufactured for one of our largest customers, we could experience a significant reduction in our revenue. Also, the insolvency of one or more of our largest customers or the inability of one or more of our largest customers to pay for its orders could decrease revenue. As many of our costs and operating expenses are relatively fixed, a reduction in net revenue can decrease our profit margins and adversely affect our business, financial condition and results of operations.

Shortages or price fluctuations of component parts specified by our customers could delay product shipment and affect our profitability.

A substantial portion of our revenue is derived from turnkey manufacturing. In turnkey manufacturing, we provide both the materials and the manufacturing services. If we fail to manage our inventory effectively, we may bear the risk of fluctuations in materials costs, scrap and excess inventory, all of which can have an adverse impact on our business, financial condition and results of operations. In addition, delays, cancellations or reductions of orders by our customers could result in an excess of materials. Orders received from customers within component lead time, rapid increases in orders or lengthening of lead times by suppliers could cause a shortage of materials. A shortage of materials could lengthen production schedules and increase costs. An excess of materials may increase the costs of maintaining inventory and may increase the risk of inventory obsolescence, both of which may increase expenses and decrease profit margins and operating income.

Many of the products we manufacture require one or more components that we order from sole-source suppliers. Supply shortages for a particular component can delay production of all products using that component or cause cost increases in the services we provide. In addition, in the past, some of the materials we use, such as memory and logic devices, have been subject to industry-wide shortages. As a result, suppliers allocate available quantities among their customers, and we have not been able to obtain all of the materials required. Our inability to obtain these materials could slow production or assembly, delay shipments to our customers, increase costs and reduce operating income. During fiscal year 2010, the Company has been experiencing an increase in lead times

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due to the effect of industry wide component shortages. Also, we may bear the risk of periodic component price increases, which could reduce operating income. Also we rely on a variety of common carriers for materials transportation, and we route materials through various world ports. A work stoppage, strike or shutdown of a major port or airport could result in manufacturing and shipping delays or expediting charges, which could have an adverse impact on our business, financial condition and results of operations.

Our indebtedness could adversely affect our financial health and severely limit our ability to plan for or respond to changes in our business.

On May 18, 2010, the Company and its lenders signed an amendment to extend the term of the debt agreement to July 2013, and to reset the EBITDA and leverage covenants, along with interest rates and the repayment schedule. The revolving line of credit now bears interest at prime to prime plus 1%, the term loan to EDC now bears interest at LIBOR plus 2.5% to 3.5%, and the term loan to Wells Fargo now bears interest at LIBOR plus 3% to 4%, depending on a grid as specified in the debt agreement, which decreases as increasing rolling four-quarter EBITDA levels are achieved. Under the new amendment, repayments of the term loan to EDC for fiscal 2010 are postponed. Payments are scheduled to recommence on April 1, 2011. Management believes that the Company will be in compliance with these amended covenants for the foreseeable future. Accordingly, the outstanding balances under the lending agreements continue to be classified as long-term. Continued compliance with its covenants, however, is dependent on the Company achieving certain forecasts. While management is confident in its plans, market conditions have been difficult to predict and there is no assurance that the Company will achieve its forecasts.

Our debt under the Wells Fargo EDC Facilities could have adverse consequences for our business, including:

- We will be more vulnerable to adverse general economic conditions.
- We will be required to dedicate a substantial portion of our cash flow from operations to repayment of debt, limiting the availability of cash for other purposes.
- We may have difficulty obtaining financing in the future for working capital, capital expenditures, acquisitions, general corporate purposes or other purposes.
- We may have limited flexibility in planning for, or reacting to, changes in our business and industry.
- We could be limited in our borrowing of additional funds and making strategic investments by restrictive covenants and the borrowing base formula in our credit arrangements.
- We may fail to comply with covenants under which we borrowed our indebtedness, including various financial covenants under our Wells Fargo EDC Facilities. These covenants, applicable to specific four quarter rolling periods, include (i) a minimum consolidated EBITDA target, (ii) a maximum total debt to EBITDA ratio, and (iii) maximum capital expenditures. Our failure to comply with covenants could result in an event of default. If an event of default occurs and is not cured or waived, it could result in all amounts outstanding, together with accrued interest, becoming immediately due and payable. If we were unable to repay such amounts, our lenders could proceed against any collateral granted to them to secure that indebtedness. There can be no assurance that we will maintain compliance with the covenants under the Wells Fargo EDC Facilities.
- Our Wells Fargo EDC Facilities contains subjective acceleration clauses. There can be no assurance that the lender will not exercise their rights to accelerate repayment under the terms of the agreement.

There can be no assurance that our leverage and such restrictions will not materially adversely affect our ability to finance our future operations or capital needs or to engage in other business activities. In addition, our ability to pay principal and interest on our indebtedness to meet our financial and restrictive covenants and to satisfy our other debt obligations will depend upon our future operating performance, which will be

affected by prevailing economic conditions and financial, business and other factors, certain of which are beyond our control, as well as the availability of revolving credit borrowings under the Wells Fargo EDC Facilities or successor facilities.

Item 6 Exhibits

10.1	Employment Agreement Amendment dated as at November 10, 2010 between John Caldwell and SMTC Manufacturing Corporation of Canada.
31.1	Certification of John Caldwell pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated November 12, 2010.
31.2	Certification of Jane Todd pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated November 12, 2010.
32.1	Certification of John Caldwell, pursuant to Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, dated November 12, 2010.
32.2	Certification of Jane Todd, pursuant to Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, dated November 12, 2010.

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SIGNATURES

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

SMTC CORPORATION

By:	/s/ JOHN CALDWELL
Name:	**John Caldwell**
Title:	**President and CEO**
By	/s/ JANE TODD
Name:	**Jane Todd**
Title:	**Chief Financial Officer**

Date: November 12, 2010

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