

KEY TRONIC CORP
Form 10-K
September 10, 2018

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

FORM 10-K

x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
FOR THE FISCAL YEAR ENDED JUNE 30, 2018

OR
.. TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF
1934
FOR THE PERIOD FROM TO
Commission File Number 0-11559

KEY TRONIC CORPORATION
(Exact name of registrant as specified in its charter)

Washington (State or other jurisdiction of Incorporation or organization)	91-0849125 (I.R.S. Employer Identification No.)
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N. 4424 Sullivan Road, Spokane Valley, Washington (Address of principal executive offices)	99216 (Zip Code)
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(509) 928-8000
(Registrant's telephone number, including area code)

N/A
(Former name, former address and former fiscal year, if changed since last report)

Securities Registered Pursuant to Section 12(b) of the Act: None

Title of each class Common stock, no par value	Name of each exchange on which registered The NASDAQ Stock Market LLC
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Securities Registered Pursuant to Section 12(g) of the Act: None

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

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

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes 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 Regulations 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, 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.

(Check one):

Large accelerated filer Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

Emerging growth company

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

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

State the aggregate market value of the voting and non-voting common equity held by non affiliates computed by reference to the price at which the common equity was last sold, or the average bid and asked price of such common equity, as of the last business day of the registrant's most recently completed second fiscal quarter.

As of December 30, 2017, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was \$69.5 million based on the closing price as reported on the NASDAQ.

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 10,759,680 shares of common stock were outstanding as of September 4, 2018.

Documents Incorporated by Reference:

Certain information is incorporated into Part III of this report by reference to the Proxy Statement for the registrant's 2018 annual meeting of stockholders to be filed with the Securities and Exchange Commission pursuant to Regulation 14A not later than 120 days after the end of the fiscal year covered by this Form 10-K.

KEY TRONIC CORPORATION
2018 FORM 10-K
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FORWARD-LOOKING STATEMENTS

References in this report to “the Company,” “Key Tronic,” “KeyTronicEMS,” “we,” “our,” or “us” mean Key Tronic Corporation together with its subsidiaries, except where the context otherwise requires.

This Annual Report on Form 10-K contains forward-looking statements in addition to historical information.

Forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those reflected in the forward-looking statements. Risks and uncertainties that might cause such differences include, but are not limited to those outlined in “Management’s Discussion and Analysis of Financial Condition and Results of Operations—Risks and Uncertainties that May Affect Future Results.” Readers are cautioned not to place undue reliance on forward-looking statements, which reflect management’s opinions only as of the date hereof. The Company undertakes no obligation to update forward-looking statements to reflect developments or information obtained after the date hereof and disclaims any obligation to do so. Readers should carefully review the risk factors described in periodic reports the Company files from time to time with the Securities and Exchange Commission, including Quarterly Reports on Form 10-Q and Current Reports on Form 8-K.

PART I

Item 1. BUSINESS

Background

Key Tronic Corporation (dba: KeyTronicEMS Co.) was organized in 1969, as a Washington corporation that locally manufactured computer keyboards. The ability to design, build and deliver a quality product led us to become a leading independent manufacturer of keyboards for computers in the United States. Our fully integrated design, tooling, and automated manufacturing capabilities enabled us to rapidly respond to customers’ needs for keyboards in production quantities worldwide. We supported our sales growth through the development and purchase of international manufacturing facilities. As the computer keyboard market matured with increasing competition from other international providers, we determined that our business could no longer solely rely on keyboard sales.

After assessing market conditions and our strengths and capabilities, we shifted our focus from keyboard manufacturing to contract manufacturing for a wide range of products. Our unique strategic attributes are based on our core strengths of innovative design and engineering expertise in electronics, mechanical engineering, sheet metal fabrication and stamping, and precision plastics combined with high-quality, low cost production, and assembly on an international basis while providing exceptional customer service. These strengths have made our company a strong competitor in the electronic manufacturing services (EMS) market.

Our Industry and Strategy

The expansion of the EMS industry and our acquisitions have allowed us to continue to expand our customer base and the industries that we serve. The increase in new programs represents a growing portion of our revenue and a promising foundation for our future. In keeping with our long-term strategic objectives, we have been successfully building a more diversified customer portfolio, spanning a wider range of industries. We currently offer our customers the following services: integrated electronic and mechanical engineering, precision plastic molding, sheet metal fabrication, printed circuit board (PCB) and complete product assembly, component selection, sourcing and procurement, worldwide logistics, and new product testing and production all at competitive pricing due to our global footprint. We differentiate ourselves from others our size and larger in the EMS industry by providing vertical integration, a flexible and responsive approach to our customer’s changing supply demand, and complete design engineering support.

We believe that we are well positioned in the EMS industry to continue the expansion of our customer base and achieve long-term growth. Our unique blend of multinational facilities, vertical integration, centralized management, and core strengths continue to support our growth and our customers’ needs. We continue to focus on controlling operating expenses and leveraging the synergistic capabilities of our world-class facilities in the United States, Mexico, and China. This international production capability provides our customers with the benefits of improved supply-chain management, reduced inventory, lower labor costs, lower transportation costs, and reduced product fulfillment time. Given our competitive advantages and the growing pressure for new potential customers to move forward with their outsourcing strategies, we are strongly positioned to win new business in coming periods and grow our revenue and profits.

The EMS industry is intensely competitive. Although our customer base is growing, we still have less than 1% of the potential global market and our revenue can fluctuate significantly due to reliance on a concentrated base of customers. We are planning for new customer growth in the coming quarters by securing new programs with new and existing customers, increasing our worldwide manufacturing capacity, leveraging further our design engineering capabilities and continuing to improve our manufacturing and procurement processes and capabilities. Ongoing challenges that we face include but are not limited to the following: continuing to win programs from new and existing customers, balancing capital employed, production capacity and key personnel in support of new customer programs, improving operating efficiencies, controlling costs while developing competitive pricing strategies, and successfully transitioning new program wins to full production.

Customers and Marketing

We provide a mix of manufacturing services for outsourced Original Equipment Manufacturing (OEM) products. We provide the following EMS services: product design, surface mount technologies (SMT) and pin through hole capability for printed circuit board assembly, tool making, precision plastic molding, sheet metal fabrication and painting, liquid injection molding, complex assembly, automated tape winding, prototype design and full product assembly.

Sales of the majority of our products have not historically been seasonal in nature, but may be seasonal in the future if there are changes in the types of products manufactured. Sales can, however, fluctuate significantly between quarters from changes in customers and customer demand due to the concentration of sales generated by our largest customers. For the fiscal years 2018, 2017 and 2016, the five largest customers in each year accounted for 42%, 42% and 41% of combined total net sales, respectively. We continue to diversify our customer base by adding additional programs and customers. We expect net sales to our five largest customers as a percentage of total net sales to approximate current levels going forward.

The following table represents all customers that represented 10% or more of total net sales during the last three fiscal years:

	Percentage of Net Sales by Fiscal Year		
	2018	2017	2016
Customer A	19%	18%	18%

There can be no assurance that the Company's principal customers will continue to purchase products from the Company at current levels. Moreover, the Company typically does not enter into long-term volume purchase contracts with its customers, and the Company's customers have certain rights to extend or delay the shipment of their orders. The loss of one or more of the Company's major customers, or the reduction, delay or cancellation of orders from such customers, could materially and adversely affect the Company's business, operating results and financial condition. We market our products and services primarily through our direct sales department which is comprised of strategically located field sales people and distributors. We also maintain relationships with several independent sales organizations to assist in marketing our EMS product lines.

Manufacturing

We have continually made investments in developing and expanding a capital equipment base to achieve vertical integration and efficiencies in our manufacturing processes. We have invested significant capital into SMT for volume manufacturing of complex printed circuit board assemblies and in our metal shop providing precision metal stamping, fabricating, and finishing. We also design and develop tooling for injection molding and sheet metal fabrication and manufacture the majority of plastic and sheet metal parts used in the products we manufacture. Additionally, we have equipment to maintain a controlled clean environment for manufacturing processes that require a high level of precise control.

We use a variety of manual and automated assembly processes in our facilities, depending upon product complexity and degree of customization. Some examples of automated processes include component insertion, SMT, selective soldering, flexible robotic assembly, automated storage tape winding, computerized vision system quality inspection, laser turrets, automated switch and key top installation, robotic welding, automated powder coat application, and automated functional testing.

Our engineering expertise and automated manufacturing processes enable us to work closely with our customers during the design and prototype stages of production and to jointly increase productivity and reduce response time to the marketplace. We use computer-aided design techniques and software to assist in preparation of the tool design layout and component placement, to reduce tooling and production costs, improve component and product quality, and enhance turnaround time during product development.

We purchase materials and components for our products from many different suppliers, including both domestic and international sources. We develop close working relationships with our suppliers, many of whom have been supplying products to us for several years.

Research, Development, and Engineering

As part of our long-term strategy, we are committed to supporting our customers by providing research, development, and engineering services. We have recently seen an increase in the success of providing design support on existing and potential customers in differentiating ourselves. These services allow us to facilitate in optimizing new product designs, and the production processes of our customers' programs.

Research, development, and engineering (RD&E) expenses consist principally of employee related costs, third party development costs, program materials costs, depreciation, and allocated information technology and facilities costs.

Competition

The market for the products and services we provide is highly competitive. There are numerous competitors in the EMS industry, many of which have substantially more resources and are more geographically diverse than we are. Some of our competitors have similar international production capabilities, large financial resources and some have substantially greater manufacturing, research and development, and marketing resources. There is also competition from the manufacturing operations of our current and potential customers, who are continually evaluating the merits of manufacturing their products internally versus the advantages of outsourcing. We believe that we can currently compete favorably in these areas primarily on the basis of our international footprint, responsiveness, creativity, vertical production capability, quality, and cost.

Trademarks

Our name and logo are federally registered trademarks, and we believe they are valuable assets of our business. We operate under the trade name "KeyTronicEMS" to better identify our primary business concentration in contract manufacturing in the EMS industry.

Employees

We consider our employees to be our primary strength and we make considerable efforts to maintain a well-qualified workforce. Our employee benefits include bonus programs involving periodic payments to all employees based on meeting quarterly or fiscal year performance targets. We regularly provide transportation, medical services, and meals to all of our employees in foreign locations. The Company also has defined contribution plans available to U.S. employees who have attained age 21 and provide group health, life, and disability insurance plans. We also maintain share based compensation plans and other long-term incentive plans for certain employees and outside directors. As of June 30, 2018 we had 4,701 full-time employees compared to 5,038 on July 1, 2017, and 4,947 on July 2, 2016. Since we can have significant fluctuations in product demand, we seek to maintain flexibility in our workforce by utilizing skilled temporary labor in our manufacturing facilities in addition to full-time employees.

Backlog

On July 28, 2018 our order backlog was valued at approximately \$167.7 million, compared to approximately \$126.9 million on July 29, 2017. The amount of backlog is not necessarily indicative of future sales but can be indicative of trends in expected future sales revenue. Due to the relationships with our customers, we will occasionally allow orders to be canceled or rescheduled and as a result it is not a meaningful indicator of future financial results. If there are canceled or rescheduled orders, we typically negotiate fees to cover the costs we have incurred. Order backlog consists of purchase orders received for products expected to be shipped approximately within the next twelve months, although shipment dates are subject to change due to design modifications, customer forecast changes, or other customer requirements.

Foreign Markets

Information concerning net sales and long-lived assets (property, plant, and equipment) by geographic areas is set forth in Note 12, "Enterprise-Wide Disclosures" of the consolidated financial statements of this Annual Report on Form 10-K and that information is incorporated herein.

Executive Officers of the Registrant

The table below sets forth the name, current age and current position of our executive officers and other significant employees:

Name	Age	Positions Held
Executive Officers		
Craig D. Gates	59	President and Chief Executive Officer
Brett R. Larsen	45	Executive Vice President of Administration, Chief Financial Officer, and Treasurer
Douglas G. Burkhardt	60	Executive Vice President of Worldwide Operations
Philip S. Hochberg	56	Executive Vice President of Business Development
David H. Knaggs	37	Vice President of Quality and Regulatory Affairs
Frank Crispigna III	57	Vice President of Supply Chain
Duane D. Mackleit	50	Vice President of Program Management
Chad T. Orebaugh	47	Vice President of Engineering

Executive Officers

CRAIG D. GATES – President and Chief Executive Officer

Mr. Gates, age 59, has been President and Chief Executive officer of the Company since April 2009. Previously, he was Executive Vice President and General Manager from August 2002 to April 2009. He served as Executive Vice President of Marketing, Engineering and Sales from July 1997 to August 2002 and served as Vice President and General Manager of New Business Development from October 1995 to July 1997. He joined the Company as Vice President of Engineering in October of 1994. From 1982 to 1991 he held various engineering and management positions within the Microswitch Division of Honeywell, Inc., in Freeport, Illinois, and from 1991 to October 1994 he served as Director of Operations, Electronics for Microswitch. Mr. Gates has a Bachelor of Science Degree in Mechanical Engineering and a Masters in Business Administration from the University of Illinois, Urbana.

BRETT R. LARSEN – Executive Vice President of Administration, Chief Financial Officer, and Treasurer

Mr. Larsen, age 45, has served as Executive Vice President of Administration, Chief Financial Officer, and Treasurer since July 2015. Previously, he was Vice President of Finance and Controller from February 2010 to July 2015. He was Chief Financial Officer of FLSmidth Spokane, Inc. from December 2008 to February 2010. From October 2005 through November 2008, Mr. Larsen served as Controller of Key Tronic Corporation. From May 2004 to October 2005, Mr. Larsen served as Manager of Financial Reporting of Key Tronic Corporation. From 2002 to May 2004, Mr. Larsen was an audit manager for the public accounting firm BDO USA, LLP. He also held various auditing and supervisory positions with Grant Thornton LLP from 1997 to 2002. Mr. Larsen has a Bachelor of Science degree in Accounting and a Masters degree in Accounting from Brigham Young University and is a Certified Public Accountant.

DOUGLAS G. BURKHARDT – Executive Vice President of Worldwide Operations

Mr. Burkhardt, age 60, has been Executive Vice President of Worldwide Operations of the Company since July 2010. Previously Mr. Burkhardt was Vice President of Worldwide Operations from July 2008 to July 2010 and Director of China Operations and Program Management from January 2006 to July 2008. Mr. Burkhardt also served as Director of Northwest and China Operations from November of 1998 to January of 2006. Mr. Burkhardt also served as Director of Customer Satisfaction from March 1997 to November 1998 and Director of Molding from September of 1995 to March of 1997. Prior to this, Mr. Burkhardt served in other various senior management positions within the Company. Mr. Burkhardt has been with the Company since May of 1989. Prior to joining Key Tronic, Mr. Burkhardt worked for House of Aluminum and Glass for 12 years where he was the plant manager.

PHILIP S. HOCHBERG – Executive Vice President of Business Development

Mr. Hochberg, age 56, has been Executive Vice President of Business Development since July 2012. Prior to this, Mr. Hochberg served as Vice President of Business Development from October 2009 through June 2012. He was Director of Business Development and Program Management from July 2008 to October 2009. Mr. Hochberg served as Director of Business Development from October 2004 to July 2008 and as Director of EMS Sales and Marketing from July 2000 to October 2004. Prior to joining Key Tronic, Mr. Hochberg worked for Quinton Instrument Company as their Director of Marketing and Product Management from 1992 to 2000. From 1988 to 1992, he was employed by SpaceLabs Medical as their Business Development Marketing Manager. Mr. Hochberg has an MBA from the

University of British Columbia, a BA in Psychology, with a minor in Business from Washington University in St. Louis.

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DAVID H. KNAGGS – Vice President of Quality and Regulatory Affairs

Mr. Knaggs, age 37, has been Vice President of Quality and Regulatory Affairs since October 2016. Before joining KeyTronicEMS, Mr. Knaggs worked at Telect, Inc. from 2008 to 2016 as their Director of Engineering. Prior to that, he worked at Isothermal Systems Research as Lead Systems Engineer from 2003 to 2008. He has a Bachelor of Science degree in Mechanical Engineering with a minor in mathematics from the University of Washington.

FRANK CRISPIGNA III – Vice President of Supply Chain

Mr. Crispigna, age 57, has been Vice President of Supply Chain of the company since October 2011. Prior to this, Mr. Crispigna held a variety of Materials and Supply Chain positions at Plexus Corporation since 1997, most recently serving as the Director – Supply Chain Solutions from 2005 - 2011. He has a Masters degree in Business Administration, and a Bachelor of Business Administration Degree in Marketing from the University of Wisconsin – Oshkosh. Mr. Crispigna also is a C.P.M., and received his certification in Supply Chain Leadership from the University of Wisconsin.

DUANE D. MACKLEIT – Vice President of Program Management

Mr. Mackleit, age 50, has been Vice President of Program Management of the company since July 2012. He served as Director of Program Management from July 2008 through June 2012. From May 2006 to July 2008 he served as Principal Program Manager. Prior to that, he served as Program Manager from March 2002 to May 2006 and Associate Program Manager from August 2000 to March 2002. Mr. Mackleit has also held several other positions with Key Tronic Corporation. Mr. Mackleit has an AA in Business from Spokane Falls Community College and a BA in Business/Marketing from Eastern Washington University. He also holds a MBA from Gonzaga University.

CHAD T. OREBAUGH – Vice President of Engineering

Mr. Orebaugh, age 47, has been Vice President of Engineering since April 2017. Prior to this, Mr. Orebaugh served as Director of Engineering since May 2013. From April 2010 to May 2013, he served as Manager of Engineering. From January 2000 to April 2010 he served as Lead Mechanical Engineer. Prior to that, he served as Mechanical Engineer from October 1998 to January 2000 and Associate Mechanical Engineer since October 1997. Mr. Orebaugh holds a BA in Mechanical Engineering from Gonzaga University.

Available Information

Our principal executive offices are located at 4424 North Sullivan Road, Spokane Valley, Washington 99216, and our telephone number is (509) 928-8000. Our website is located at <http://www.keytronic.com> where filings of our Annual Report on Form 10-K, Quarterly Reports on Form 10-Q or current reports on Form 8-K are available after they have been filed with the Securities and Exchange Commission. The information presented on our website currently and in the future is not considered to be part of this document or any document incorporated by reference in this document.

Item 1A. RISK FACTORS

There are risks and uncertainties that could affect our business. These risks and uncertainties include but are not limited to, the risk factors described below, in Item 7A: “Quantitative and Qualitative Disclosures about Market Risk” and elsewhere in this Form 10-K.

RISKS AND UNCERTAINTIES THAT MAY AFFECT FUTURE RESULTS

The following risks and uncertainties could affect our actual results and could cause results to differ materially from past results or those contemplated by our forward-looking statements. When used herein, the words “expects,” “believes,” “anticipates” and other similar expressions are intended to identify forward-looking statements.

We may experience fluctuations in quarterly results of operations.

Our quarterly operating results have varied in the past and may vary in the future due to a variety of factors, including adverse changes in the U.S. and global macroeconomic environment, volatility in overall demand for our customers’ products, success of customers’ programs, timing of new programs, new product introductions or technological advances by us, our customers and our competitors, and changes in pricing policies by us, our customers, our suppliers, and our competitors. Our customer base is diverse in the markets they serve, however, decreases in demand, particularly from customers in certain industries could affect future quarterly results. Additionally, our customers could be adversely impacted by illiquidity in the credit markets which could directly impact our operating results.

Component procurement, production schedules, personnel and other resource requirements are based on estimates of customer requirements. Occasionally, our customers may request accelerated production that can stress resources and reduce operating margins. Conversely, our customers may abruptly lower or cancel production which may lead to a sudden, unexpected increase in inventory or accounts receivable for which we may not be reimbursed even when under contract with customers. In addition, because many of our operating expenses are relatively fixed, a reduction in customer demand can harm our gross profit and operating results. The products which we manufacture for our customers have relatively short product life cycles. Therefore, our business, operating results and financial condition are dependent in a significant way on our ability to obtain orders from new customers and new product programs from existing customers.

Operating results can also fluctuate if changes are made to significant estimates and assumptions. Significant estimates and assumptions include the allowance for doubtful receivables, provision for obsolete and non-saleable inventory, stock-based compensation, the valuation allowance on deferred tax assets, valuation of goodwill, impairment of long-lived assets, long-term incentive compensation accrual, the provision for warranty costs, the impact of hedging activities and purchase price allocation.

We are exposed to general economic conditions, which could have a material adverse impact on our business, operating results and financial condition.

Adverse economic conditions and uncertainty in the global economy such as unstable global financial and credit markets, inflation, tariffs, and recession can negatively impact our business. Unfavorable economic conditions could affect the demand for our customers’ products by triggering a reduction in orders as well as a decline in forecasts which could adversely affect our sales in future periods. Additionally, the financial strength of our customers and suppliers and their ability to obtain and rely on credit financing may affect their ability to fulfill their obligations to us and have an adverse effect on our financial results.

The majority of our sales come from a small number of customers and a decline in sales to any of these customers could adversely affect our business.

At present, our customer base is concentrated and could become more or less concentrated. There can be no assurance that our principal customers will continue to purchase products from us at current levels. Moreover, we typically do not enter into long-term volume purchase contracts with our customers, and our customers have certain rights to extend or delay the shipment of their orders. We, however, typically require that our customers contractually agree to buy back inventory purchased within specified lead times to build their products if not used.

The loss of one or more of our major customers, or the reduction, delay or cancellation of orders from such customers, due to economic conditions or other forces, could materially and adversely affect our business, operating results and financial condition. The contraction in demand from certain industries could impact our customer orders and have a negative impact on our operations over the foreseeable future. Additionally, if one or more of our customers were to become insolvent or otherwise unable to pay for the manufacturing services provided by us, our operating results and

financial condition would be adversely affected.

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We depend on a limited number of suppliers for certain components that are critical to our manufacturing processes. A shortage of these components or an increase in their price could interrupt our operations and result in a significant change in our results of operations.

We are dependent on many suppliers, including sole source suppliers, to provide key components and raw materials used in manufacturing customers' products. We have seen supply shortages in certain electronic components. In addition, our suppliers' facilities may also experience earthquakes, tsunamis and other natural disasters which may cause a shortage of components. This can result in longer lead times and the inability to meet our customers request for flexible production and extended shipment dates. If demand for components outpaces supply, capacity delays could affect future operations. Delays in deliveries from suppliers or the inability to obtain sufficient quantities of components and raw materials could cause delays or reductions in shipment of products to our customers which could adversely affect our operating results and damage customer relationships.

We operate in a highly competitive industry; if we are not able to compete effectively in the EMS industry, our business could be adversely affected.

Competitors may offer customers lower prices on certain high volume programs. This could result in price reductions, reduced margins and loss of market share, all of which would materially and adversely affect our business, operating results, and financial condition. If we were unable to provide comparable or better manufacturing services at a lower cost than our competitors, it could cause sales to decline. In addition, competitors can copy our non-proprietary designs and processes after we have invested in development of products for customers, thereby enabling such competitors to offer lower prices on such products due to savings in development costs.

Cash and cash equivalents are exposed to concentrations of credit risk.

We place our cash with high credit quality institutions. At times, such balances may be in excess of the federal depository insurance limit or may be on deposit at institutions which are not covered by insurance. If such institutions were to become insolvent during which time it held our cash and cash equivalents in excess of the insurance limit, it could be necessary to obtain other credit financing to operate our facilities.

Our ability to secure and maintain sufficient credit arrangements is key to our continued operations.

There is no assurance that we will be able to retain or renew our credit agreements in the future. In the event the business grows rapidly or there is uncertainty in the macroeconomic climate, additional financing resources could be necessary in the current or future fiscal years. There is no assurance that we will be able to obtain equity or debt financing at acceptable terms, or at all in the future. In addition, we have restrictive covenants with our financial institution which could impact how we manage our business. If we cannot meet our financial covenants, our borrowings could become immediately payable which could have a material adverse impact on our financial statements. For a summary of our banking arrangements, see Note 4 Long-Term Debt of the "Notes to Consolidated Financial Statements."

Our operations may be subject to certain risks.

We manufacture product in facilities located in Mexico, China and the United States. These operations may be subject to a number of risks, including:

- difficulties in staffing, turnover and managing onshore and offshore operations;
- political and economic instability (including acts of terrorism, pandemics, civil unrest, forms of violence and outbreaks of war), which could impact our ability to ship, manufacture, and/or receive product;
- unexpected changes in regulatory requirements and laws;
- longer customer payment cycles and difficulty collecting accounts receivable;

\$ \$ 89,417

* T. Rowe Price Stable Fund seeks to maximize current income consistent with the maintenance of principal and to provide for withdrawals for certain participant initiated transactions under a retirement plan without penalty or adjustment. There are no unfunded commitments, redemption frequency restrictions, or other redemption restrictions.

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The following table sets forth by level within the fair value hierarchy a summary of the Plan's assets measured at fair value on a recurring basis as of December 31, 2010 (amounts in thousands):

	Level 1	Level 2	Level 3	Total
Balanced mutual funds	\$ 10,782	\$	\$	\$ 10,782
Fixed income mutual funds	5,241			5,241
Growth mutual funds	43,803			43,803
Common stock of KEMET Corporation	8,246			8,246
T. Rowe Price Stable Value Fund*		23,918		23,918
	\$ 68,072	\$ 23,918	\$	\$ 91,990

* T. Rowe Price Stable Value Fund seeks to maximize current income consistent with the maintenance of principal and to provide for withdrawals for certain participant initiated transactions under a retirement plan without penalty or adjustment. There are no unfunded commitments, redemption frequency restrictions, or other redemption restrictions.

(4) Related Party Transactions

Certain Plan investments are shares of mutual funds and a stable value fund managed by T. Rowe Price. T. Rowe Price is the trustee as defined by the Plan; and therefore, these transactions qualify as party-in-interest. Fees paid by the Plan to T. Rowe Price for loan administration services were \$4,148 and \$2,203 for the years ended December 31, 2011 and 2010, respectively. The Company pays for the annual audit and all legal and fiduciary related services related to the Plan. The Plan also has investments in common stock of KEMET Corporation.

(5) Plan Termination

Although it has not expressed any intent to do so, the Company has the right under the Plan to amend it from time to time, to discontinue its contributions at any time, and to terminate the Plan subject to the provisions of ERISA. In the event of Plan termination, participants will remain 100% vested in their accounts.

(6) Tax Status

The Company applied for and received a determination letter dated July 7, 2010, that the Plan and related trust are designed in accordance with applicable sections of the Internal Revenue Code (IRC). The Plan has been amended since receiving the determination letter. However, the Plan s administrative committee believes that the Plan is designed and is currently being operated in compliance with the applicable provisions of the IRC.

GAAP requires Plan management to evaluate tax positions taken by the Plan and recognize a tax liability (or asset) if the Plan has taken an uncertain position that more likely than not would not be sustained upon examination by the IRS. The Plan administrator has analyzed the tax positions taken by the Plan, and has concluded that as of December 31, 2011 and 2010, there are no uncertain positions taken or expected to be taken that would require recognition of a liability or disclosure in the financial statements. The Plan is subject to routine audits by taxing jurisdictions; however, there are currently no audits for any tax periods in progress. The Plan administrator believes it is no longer subject to income tax examinations for years prior to 2008.

(7) Investments

At December 31, 2011 and 2010, the investments of the Plan were as follows, with items comprising more than 5% of net assets available for benefit separately stated (amounts in thousands):

	2011		2010
Investments at fair value:			
At quoted market prices:			
Registered investment companies (mutual funds):			
T. Rowe Price Mid-Cap Growth Fund	\$ 11,598	\$	12,068
T. Rowe Price Equity Income Fund	9,212		9,776
T. Rowe Price Balanced Fund	8,076		8,265
T. Rowe Price Small Cap Value Fund	6,920		7,215
T. Rowe Price Blue Chip Growth Fund	4,617		4,654
All other funds	19,567		17,848
	59,990		59,826
Common stock of KEMET Corporation	3,323		8,246
At estimated fair value:			
T. Rowe Price Stable Value Fund	26,104		23,918
Total investments, at fair value	\$ 89,417	\$	91,990

During the years ended December 31, 2011 and 2010, the Plan s investments appreciated (depreciated) in value as follows (amounts in thousands):

	2011		2010
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Registered investment companies (mutual funds)	\$	(2,691)	\$	7,943
Common stock of KEMET Corporation		(3,530)		6,615
	\$	(6,221)	\$	14,558

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The difference between the fair value and contract value of this Plan's fully benefit responsive investment contracts during the years ended December 31, 2011 and 2010 is reflected below (amounts in thousands):

	2011		2010
Net assets at fair value	\$ 26,104	\$	23,918
Adjustment to contract value	(910)		(864)
Net assets at contract value	\$ 25,194	\$	23,054

(8) Reconciliation of Financial Statements to Form 5500

The following is a reconciliation of net assets available for benefits per the financial statements to the Form 5500 (amounts in thousands):

	2011		2010
Net assets available for benefits per the financial statements	\$ 89,742	\$	92,249
Adjustment from the fair value to the contract value for fully benefit- responsive investment contracts	910		864
Net assets available for benefits per the Form 5500	\$ 90,652	\$	93,113

The following is a reconciliation of investment income per the financial statements to the Form 5500 (amounts in thousands):

	Year Ended December 31, 2011
Total investment loss and notes receivable interest income per the financial statements	\$ (3,363)
Net change in the fair value to the contract value for fully benefit- responsive investment contracts	46
Total investment loss per the Form 5500	\$ (3,317)

(9) Risks and Uncertainties

The Plan invests in various investment securities. Investment securities are exposed to various risks such as interest rate, market and credit risk. Due to the level of risk associated with certain investment securities it is at least reasonably possible that changes in the values of investment securities will occur in the near term and that such changes could materially affect participants' account balances and the amounts reported in the statement of net assets available for benefits.

KEMET EMPLOYEES SAVINGS PLAN

EIN #06-1198308 Plan #001

Schedule H, Line 4i Schedule of Assets (Held at End of Year)

December 31, 2011

(amounts in thousands)

(a)	(b)	(c)	(d)	(e)
Party-in-interest	Identifier of issue, borrower, lessor, or similar party	Description of investment including maturity date, rate of interest, collateral, par or maturity value	Cost	Current value
*	T. Rowe Price	American Century Diversified Bond Inv	**	\$ 966
*	T. Rowe Price	Balanced Fund	**	8,076
*	T. Rowe Price	Blue Chip Growth Fund	**	4,617
*	T. Rowe Price	Equity Income Fund	**	9,212
*	T. Rowe Price	International Stock Fund	**	3,160
*	T. Rowe Price	Mid-Cap Growth Fund	**	11,598
*	T. Rowe Price	Retirement Income Fund	**	94
*	T. Rowe Price	Retirement 2005 Fund	**	118
*	T. Rowe Price	Retirement 2010 Fund	**	611
*	T. Rowe Price	Retirement 2015 Fund	**	588
*	T. Rowe Price	Retirement 2020 Fund	**	2,313
*	T. Rowe Price	Retirement 2025 Fund	**	1,473
*	T. Rowe Price	Retirement 2030 Fund	**	1,885
*	T. Rowe Price	Retirement 2035 Fund	**	737
*	T. Rowe Price	Retirement 2040 Fund	**	631
*	T. Rowe Price	Retirement 2045 Fund	**	400
*	T. Rowe Price	Retirement 2050 Fund	**	116
*	T. Rowe Price	Retirement 2055 Fund	**	7
*	T. Rowe Price	Science & Technology Fund	**	2,415
*	T. Rowe Price	Small Cap Value Fund	**	6,920
*	T. Rowe Price	Spectrum Income Fund	**	4,053
*	T. Rowe Price	Stable Value Fund, at contract value	**	25,194
*	KEMET Corp.	Kemet Corporation Common Stock	**	3,323
	Participants	Loans, interest rates ranging from 4.25% to 9.25%***		1,235
				\$ 89,742

* A party-in-interest as defined by ERISA.

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** Cost omitted for participant-directed investments.

*** The accompanying financial statements classify participant loans as notes receivable from participants.

See accompanying report of independent registered public accounting firm.

Exhibit Index

Exhibit Number	Description
23.1	Consent of Independent Registered Public Accounting Firm