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High Volumes Return to US

A year ago, it would have been almost laughable to mention high volumes and US production in the same breath. Despite the run-up in China's labor costs, it was still cheaper, and hence more desirable, to manufacture commodity products such as PCs and cell phones in China. Nobody was talking about assembling high-volume products in the US. Mexico maybe, but not the US. Now, as Bob Dylan once sang, "The times they are a-changin'."

Not one, not two, but three OEMs have decided to build high-volume type products in the US. **Apple**, **Lenovo** and **Google**-owned **Motorola Mobility** are all putting some of their mass production in a US location. In one case, an EMS provider will handle US manufacturing, and in a second case a manufacturing partner will likely be involved. So far, Apple has not been forthcoming with its rationale for manufacturing in the US, but it appears that Motorola Mobility and Lenovo have decided on US production for reasons other than cost.

At last month's D: All Things Digital conference, Dennis Woodside, CEO of Motorola Mobility, revealed that the company's new Moto X product will be the first smartphone to be built in the US. Available this summer, every Moto X sold in the US will be assembled in Forth Worth, TX, Motorola Mobility stated on its website. The PR statement also noted that **Flextronics** remains Motorola's global manufacturing partner (Flextronics recently took over Motorola operations in China and Brazil) and that Flextronics is hiring for a new facility in Forth Worth. Woodside reported that the facility will employ 2,000 people before August.

Two days after Woodside's announcement, Flextronics CEO Mike McNamara confirmed in a meeting with analysts that the provider has been working on a 480,000-ft^2 operation in Fort Worth and is in the process of scaling up the workforce there to about 2,000 people. (Last month on p. 7, *MMI* reported that leased space of about that size was being renovated for Flextronics in Fort Worth.) McNamara said, "This will be our mainstream assembly operation for the Moto X product."

According to Motorola Mobility, there are several advantages to having its Illinois- and California-based designers and engineers much closer to its factory. "For instance, we'll be able to iterate on design much faster, create a leaner supply chain, respond much more quickly to purchasing trends and demands, and deliver devices to people here much more quickly," the company stated.

"When your manufacturing is thousands of miles away from your engineers and your designers, you actually lose the ability to innovate. You lose the ability to make fast changes to how you're manufacturing things," said Woodside. "There's a ton of technology that's coming in around 3D printing and around much smaller run manufacturing that we think we can take advantage of right here."

Rising costs in China were not one of the reasons Motorola gave for assembling in Texas. "The costs in China keep going up. It's not a reason to go build in Texas," said McNamara.

The Fort Worth facility is no stranger to mobile phone production.

Some articles in this issue

At one time, it was used to manufacture **Nokia** phones. Offering logistical advantages, the facility is located within a foreign-trade zone along with **FedEx** and **UPS** activities. FedEx operates a regional hub at Alliance Airport within the zone, and UPS maintains a regional hub at nearby Dallas/Fort Worth International Airport.

While Flextronics will be putting the phone together in Texas, not all assembly will be done there. Woodside reported that the Moto X contains 1,100 parts, and 70% of its assembly will occur in Texas. Some subassemblies will be supplied to the Fort Worth plant.

PC production comes back to the US

This month, **Lenovo** officially opened its first PC manufacturing line in the US. Capable of turning out desktops, notebooks and other products, the line is located within an existing 240,000-ft^2 Lenovo facility in Whitsett, NC. The new line began operations in January and is on track to fully ramp up production by the end of June.

Tom Looney, VP and GM for Lenovo North America, told *NPR* that the new line gives Lenovo flexibility and speed to win in the marketplace. *NPR* cited Lenovo management as saying that it still costs less to produce computers offshore.

Lenovo's new PC operation reflects the company's in-house manufacturing strategy, which, the company says, gives it control over both product development and supply chain operations.

Apple, on the other hand, is well known for its extensive use of outsourcing. Yet Apple has also decided to start building PCs in the US. Late last year, CEO Tim Cook announced in a *Bloomberg Businessweek* interview that Apple intended to spend over $100 million this year on production of Mac computers in the US. He told the magazine that the company would not undertake this project alone (Dec. 2012, p. 8).

In May testimony before a US Senate subcommittee, Cook divulged a little bit more. He said, "We're investing $100 million to build a line of Macs in the US later this year. This product will be assembled in Texas…."

At Apple's annual developer conference this month, the company disclosed that its new cylindrical Mac Pro desktop will be assembled in the US. Putting two and two together, it would appear that the new Mac Pro will be produced in Texas. Now the question is who will be Apple's contract manufacturer for building the Mac Pro in Texas. Reportedly, an Asia-based analyst told Taiwan's *Economic Daily News* that Flextronics has landed this program. *MMI*, however, would like to some solid evidence before reaching any such conclusion.

But what can be concluded is that US manufacturing and high-volume products are no longer mutually exclusive.

Results

Starting the Year in a Small Hole

Combined Q1 sales for eight mid-tier and smaller EMS providers based in North America were off 3.3% year over year, not a great start for the year but not a terrible one either. This group of North American providers won't need a tremendous amount of growth later in the year to make up for the aggregate sales decline in Q1. They're starting the year in the hole, but it's not a big one.

What's more, their overall sales performance in Q1 compared quite favorably to that of a group of their large competitors. On a year-over-year basis, the collective sales drop for the mid-size and smaller providers was 5.5 percentage points less than the revenue decline of the six largest US-traded providers (chart below). In Q1, company size apparently was not an overall disadvantage for the mid-tier and smaller group. And they achieved a better result in spite of, or perhaps because of, being based in North America.

Q1 revenue for the mid-tier and smaller group totaled $610 million, down from $631 million in the year-earlier period. Of the eight providers in the group, only two – **Kimball Electronics Group** and **Sparton** – grew their sales from a year earlier, and both posted double-digit increases. Sparton took top honors with a 16.0% increase. **CTS Electronics Manufacturing Solutions**, **IEC Electronics** and **Key Tronic** all suffered double-digit declines from the year-ago period (Table 1, p. 3).

Compared with the prior quarter, Q1 sales for the group of eight decreased 3.2%. Again, the mid-tier and smaller providers as a whole outperformed their larger US-traded counterparts, whose combined sales sank 8.7% sequentially. Three providers – IEC Electronics, Kimball Electronics

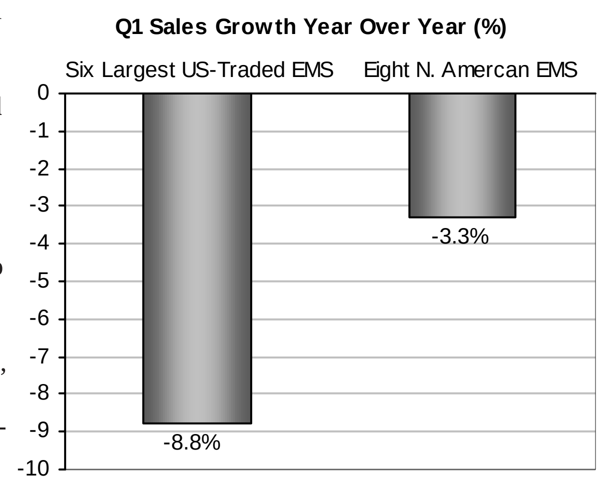

Table 1: Q1 2013 GAAP Results for Eight Mid-tier and Smaller EMS Providers Based in North America (M$ or %)

Organization	Q1 '13 sales	Q4 '12 sales	Qtr.-qtr. chg.	Q1 '12 sales	Yr.-yr. chg.	Q1 '13 gross marg.	Q4 '12 gross marg.	Q1 '12 gross marg.	Q1 '13 oper. marg.	Q4 '12 oper. marg.	Q1 '12 oper. marg.	Q1 '13 net income	Q4 '12 net income	Q1 '12 net income
Stand-Alone EMS Providers														
Key Tronic	84.3	94.6	-10.8	95.5	-11.7	9.3	10.0	9.1	4.3	5.6	4.9	2.9	3.6	3.4
SMTC	65.4	73.2	-10.5	72.5	-9.7	10.6	7.8	10.4	3.0	-1.0	4.3	1.2	1.0	2.4
Sparton	63.9	66.0	-3.2	55.0	16.0	15.7	17.3	16.6	3.5	5.3	5.8	1.5	4.4	2.0
IEC Electronics [1]	33.7	33.0	2.1	38.0	-11.4	8.6	12.6	21.3	-4.2	0.4	11.3	(1.1)	(0.1)	2.5
Nortech Systems	25.9	25.0	3.6	28.4	-8.6	12.5	14.0	10.6	0.9	1.9	1.2	0.1	0.3	0.1
Subtotal/avg.	**273.3**	**291.7**	**-6.3**	**289.4**	**-5.6**	**11.3**	**11.8**	**12.6**	**2.4**	**3.0**	**5.4**	**4.5**	**9.1**	**10.5**
EMS Units of Larger Public Companies														
Kimball Electronics Group [2]	182.1	164.2	10.9	161.0	13.1				4.9	3.0	3.1	6.5	3.9	3.3
Ducommun LaBarge Technologies	103.2	111.7	-7.6	110.1	-6.2				7.7 [3]	10.2 [3]	7.5 [3]			
CTS Electronics Manufacturing Solutions	51.5	62.6	-17.8	70.6	-27.1				2.1 [4,5]	8.9 [4,6]	0.6 [4]			
Total/avg.	**610.0**	**630.3**	**-3.2**	**631.0**	**-3.3**									

[1] IEC reported preliminary estimated results for Q1 '13 and will restate results for the previous five quarters. MMI computed gross and operating margins and net income for prior quarters by using IEC's estimated adjustments to financial statements of those quarters.
[2] Operating and net income are not necessarily equivalent to GAAP results on a stand-alone basis. [3] Segment operating income did not include corporate general and administrative expenses. [4] Segment operating income did not include corporate and shared services charges. [5] Excluded restructuring and related charges of $0.8 million not allocated to business segments. [6] Excluded restructuring and related charges of $3.8 million not allocated to business segments.

and **Nortech Systems** – managed to increase their sales sequentially, as Kimball led with a 10.9% gain.

The group of eight mid-tier and smaller providers consists of five companies in the EMS space, all publicly traded, and three EMS units within larger publicly held corporations. Together, the five stand-alone providers produced a Q1 gross margin of 11.3%, down 50 basis points sequentially and 130 basis points year over year. Three out of five providers attained double-digit gross margins, with a high of 15.7% turned in by Sparton.

In the aggregate, Q1 operating margin for the five stand-alone providers stood at 2.4%, down 60 basis points sequentially and 300 basis points year over year. Key Tronic recorded a high of 4.3%. **SMTC** was the only company able to raise its margin from the prior quarter, albeit from a negative value. In the year-over-year comparison, all five providers saw their operating margins erode (Table 1).

Among the EMS units, segment operating margins (see Table 1 footnotes) rose from a year earlier at all three units, but only Kimball Electronics boosted its margin both sequentially and year over year.

For the five stand-alone providers, net income in Q1 amounted to $4.5 million, down from $9.1 million in the prior quarter and $10.5 million in the year-ago period. Q1 net margin of 1.6% dropped 150 basis points sequentially and 200 basis points year over year. IEC alone incurred a net loss in the quarter, based on a preliminary estimated result.

Net income can also be found for one of the EMS units, Kimball Electronics. In keeping with its operating margin performance, Kimball was the only provider to lift its Q1 net income both quarter on quarter and year over year.

A brief look at each provider

CTS Electronics Manufacturing Solutions. Q1 sales of CTS's EMS unit dropped 27% year over year, primarily due to lower demand in the defense and aerospace and industrial markets, partly offset by higher sales in the communications market. Despite lower sales volume, EMS operating income before corporate and shared services charges increased to $1.1 million from $455,000 a year earlier, mainly because of lower net expenses related to the Thailand floods of 2011.

On a sequential basis, sales fell 18%, primarily as a result of weaker sales in the defense and aerospace, industrial and medical markets, partly offset by increases in the communications market. EMS operating income before corporate and shared services charges was down by $4.5 million, mainly due to flood insurance recoveries of $5.0 million received in Q4 2012 and lower sales, partly offset by lower operating costs.

Ducommun LaBarge Technologies. Ducommun's DLT segment reported Q1 sales of $103.2 million, down 6% year over year as a result of a 32% decline in Ducommun's end markets outside aerospace and defense, partly offset by a 15% increase in sales of defense technologies products.

DLT's operating income for Q1, which did not include corporate general and administrative expenses, amounted to $7.9 million, or 7.7% of revenue, compared with $8.3 million, or 7.5% of revenue, in the year-earlier period. EBITDA before certain allocated corporate overhead came in at 12.2% of sales, up 40 basis points year over year, even though EBITDA value declined slightly to $12.6 million in Q1 from $13.0 million a year earlier.

IEC Electronics. For its fiscal Q2 ended March 29, revenue declined by $4.3 million, or 11%, from the year-earlier period. Sales from the medical, industrial and communication and other market sectors fell by a total of $5.1 million, which was partly offset by a $0.8-million increase in revenue from the military and aerospace sector.

In fiscal Q2, gross margin decreased to 8.6% from 21.3% a year earlier. Lower sales volume, which reduced absorption of fixed production costs, and unfavorable changes in product mix at some locations were partly offset by higher sales volume and favorable changes in mix at others. In addition, higher labor costs were incurred in anticipation of higher revenue volumes that did not materialize in the quarter, particularly in the **Southern California Braiding** operation. The costs of resolving technical problems for a telecom customer also had a negative effect on gross profit. Finally, converting IEC's Newark, NY, location from one large operation to three smaller ones took a bite out of profitability.

A gross profit decrease of $5.2 million from the year-ago quarter and an increase in SG&A were mainly responsible for a fiscal Q2 net loss of $1.1 million, compared with net income of $2.5 million a year earlier.

IEC is in the process of revising its financial statements for the five quarters prior to fiscal Q2 due to an error in accounting for work-in-process inventory at Southern California Braiding. Since the company continues to review these matters, IEC has not yet finalized its financial statements for fiscal Q2 as of this writing.

Key Tronic. Revenue for its fiscal Q3 ended March 30 totaled $84.3 million, down 12% year over year. Net income amounted to $2.9 million, or $0.26 a share, compared with $3.4 million, of $0.32 a share, in the same period a year ago. The drop in net income was 16%.

Gross margin for the quarter stood at 9.3%, up 20 basis points year over year, while operating margin was 4.3%, down 60 basis points year over year.

Revenue in the quarter was primarily affected by an anticipated slowdown from a large customer that began to reduce production levels in the prior quarter. Continued ramp-up of new programs in fiscal Q3 did not make up for the lower demand from this customer.

The provider continues to see a robust pipeline of new business and has further diversified its future revenue base during the quarter by winning new programs involving RFID, industrial power, LED lighting and commercial washroom equipment.

For the June quarter, Key Tronic expects revenue of $83 million to $87 million and EPS of $0.21 to $0.27. The company anticipates renewed sequential growth during fiscal 2014.

Kimball Electronics Group. Parent company Kimball International was pleased with the performance of its EMS unit, Kimball Electronics Group, during the company's fiscal Q3 ended March 31. EMS sales increased 13% year over year in keeping with the growth of sales to customers in all four of Kimball Electronics' segments: automotive, medical, industrial and public safety.

The unit's gross margin improved by 140 basis points from the year-earlier quarter, mainly because of leverage gained on the higher revenue as well as benefits realized from global purchasing efforts and operating efficiencies.

As a percentage of sales, SG&A expenses for the unit increased 20 basis points year over year, as SG&A costs went up 16% from a year earlier primarily due to greater incentive compensation related to earnings improvement in the quarter.

Nortech Systems. Q1 sales of $25.9 million rose 4% sequentially but declined 9% year over year. After an impairment charge of $74,000 on a building held for sale, operating income was $224,000, down from $328,000 for the same period in 2012. The company earned net income of $141,000 with the help of reinstated of R&D tax credits. This figure compares with $123,000 reported for the year-ago period.

Ongoing productivity improvements, including initiatives in automation and lean manufacturing, helped drive profitability in the quarter as Nortech saw gross margin increase 190 basis points year over year.

The company's 90-day backlog grew 11% during the quarter, led by defense and medical customers. This is the first double-digit backlog increase in more than 18 months, which gives Nortech's CEO a reason to be optimistic for 2013.

SMTC. The provider recorded Q1 revenue of $65.4 million, down 11% sequentially and 10% year over year. Compared with expectations, the company experienced a reduction of $14 million in Q1 orders largely from two customers, which led to lower revenues and higher inventories for the quarter. Margin improvement partly offset the impact of the revenue decline.

Gross margin came in at 10.6%, up from 7.8% in the prior quarter. However, when the effects of unrealized foreign exchange on derivative instruments were removed, Q1 gross margin became 9.1% versus 8.4% in the previous period.

In Q1, SMTC earned net income of $1.2 million, up from $1.0 million in the prior quarter but down from $2.4 million a year earlier. EPS for Q1 was $0.07, while adjusted EPS was $0.04.

For 2013, the company has reduced its revenue guidance to $260 million to $275 million from $275 million to $290 million. Guidance for adjusted EPS has been lowered to $0.35 to $0.40 from $0.45 to $0.55.

SMTC said it is on track to discontinue Canadian manufacturing operations in Q2 2013.

Sparton. For its fiscal Q3 ended March 31, sales totaled $63.9 million, up 16% year over year, while net income amounted to $1.5 million, down 26% year over year. Excluding Sparton's November 2012 acquisition of **Onyx EMS**, sales declined 6% from a year earlier. EPS of $0.14 (GAAP and non-GAAP) fell short of non-GAAP EPS of $0.19 in the year-ago period due to lower foreign sonobuoy shipments in fiscal Q3 versus a year earlier. (Sonobuoys are used by US and foreign navies.)

Omitting sales from Onyx, legacy medical sales were essentially flat versus the year-earlier quarter. Excluding Onyx, gross margin of the legacy medical business rose to 13.9% from 13.3% in the same period a year ago. With all of Onyx's sales counted in the medical segment, the segment's sales climbed 45% year over year, while its gross margin was 13.6%.

Excluding a $0.5-million increase in intracompany sales, Complex Systems sales to external customers grew 37% year over year because of increased sales to the majority of this segment's customers. CS gross margin rose to 11.5% from 7.3% a year earlier, mainly reflecting greater capacity utilization and favorable product mix. Revenue from Defense and Security Systems fell 33% year over year, as gross margin decreased to 21.8% from 23.9% a year earlier.

The company said it expects a "very strong" June quarter.

Double-Digit Drop for European Group

Reflecting the weakness that has dogged European economies, combined Q1 sales for a group of six European EMS providers fell 10.5% year over year. Revenue for this group of mid-sized providers totaled 297.1 million euros, down from 332.0 million euros in the same period a year ago. Here is another case where end market softness has overridden new business from outsourcing.

The European providers' double-digit decline does not compare well with the Q1 performance of a group of eight similar-sized providers based in North America (see previous article). Combined Q1 revenue of the North American providers went down 3.3% year over year in US dollars, which was 7.2 percentage points better than the European result calculated in euros. If these results can be extrapolated, then being based in Europe was a disadvantage in Q1.

Of the six European providers, only one, **Scanfil**, managed to increase Q1 sales from the year-earlier period. Three of the others experienced double-digit drops in revenue versus a year earlier (Table 1A).

Scanfil attributed its 3% revenue growth to a positive development in the demand for professional electronics products and a broader customer base. The company's Q1 revenue totaled 44.0 million euros. Representing 81% of the Q1 total, sales to professional electronics customers were up more than 10% year over year, partly offset by a drop in telecom sales.

Operating profit for Q1 amounted to 2.0 million euros, up about 43% year over year due to cost control and the increase in sales to professional electronics customers. Operating margin came in at 4.6%, 120 basis points above the year-ago figure. Excluding nonrecurring items, the margin increase expanded to 230 basis points. Scanfil earned a net profit in Q1 of 1.1 million euros, compared with 1.2 million euros a year earlier.

The company estimates that its 2013 revenue will increase versus 2012, and that operating profit will be on par with 2012.

At **PartnerTech**, Q1 sales were SEK 553.9 million, down 9% (6% in euros) year over year but up 1% sequentially. Following a difficult Q4, the company returned to positive operating income of SEK 8.1 million, or 1.5% of sales, down from SEK 21.1 million, or 3.5% of sales, in the year-

Table 1A: Q1 2013 Results for Six European EMS Providers (M euros or %)

Company (in order of Q1 '13 sales)	Head-quarters	Reports in euros	Q1 '13 sales	Q1 '12 sales	Yr.-yr. chg.
PartnerTech	Sweden	No	65.2	69.0	-5.5
Neways Electronics International	Netherlands	Yes	63.8	73.3	-13.0
Kitron	Norway	No	50.9	59.4	-14.2
Scanfil	Finland	Yes	44.0	42.6	3.3
LACROIX Electronics	France	Yes	42.5	46.6	-8.8
Connect Group	Belgium	Yes	30.7	41.1	-25.3
Total/avg.			**297.1**	**332.0**	**-10.5**

Results in non-euro currencies were converted to euros by applying a three-month average exchange rate for the corresponding quarter. Average exchange rates were obtained from OANDA.

earlier period. The decrease in operating income was mainly caused by lower sales. For Q1, PartnerTech reported a net profit of SEK 1.8 million, compared with SEK 12.3 million a year earlier.

Sales in the company's electronics segment declined 5% year over year, mostly due to lower volumes for Information Technology, the company's largest market area. The segment's operating margin came in at 4.6%, down 20 basis points year over year. Revenue from the systems integration and enclosures segment dropped 12% year over year mainly because of a sharp decline in the IT market area, though there was growth from maritime business. This segment operated at a loss, as did the company's machining segment, whose sales fell 10% year over year.

Neways Electronics International recorded sales of 63.8 million euros in Q1, representing a drop of 13% from the year-earlier period but a gain of 6% from the prior quarter. For Q1, the company booked a slight loss excluding exceptional items, but this result was a significant improvement over Q4 2012. The provider recorded an extraordinary reorganization charge of 3.7 million euros (pretax) in Q1, reflecting the dispersal of production activities in Echt, The Netherlands, to other Neways operating companies.

An imbalance in capacity utilization across the Neways Group remained at a relatively high level in Q1 due to persistent market volatility. Distributing production activities in Echt to other units will result in improved utilization as well as cost savings and reduced investment levels, said Neways. This action will produce annual savings roughly equivalent to the reorganization charge.

Neways does not expect to see clear improvement in the EMS market in the coming months. The company does foresee that high volatility in the market will continue.

Kitron reported Q1 revenue of NOK 378.3 million, down 16% (14% in euros) from the same period in 2012. Compared with a year earlier, sales decreased in all five of the company's segments. The largest drop of 36% occurred in the Energy/Telecoms segment, where metering business has been shrinking for Kitron. Double-digit declines were also seen in two other segments, Defense/Aerospace and Industry as sales went down 20% and 17% respectively.

Operating profit (EBIT) amounted to NOK 4.0 million in Q1, which was well below the year-earlier level of NOK 21.5 million. Kitron posted a Q1 net profit of NOK 1.4 million, compared with NOK 10.0 million a year ago.

Order intake in the quarter was 20% lower than in Q1 2012, while order backlog was down 5% from a year earlier.

Kitron has reduced its revenue outlook for 2013 and now expects slightly lower sales than in 2012. To compensate for a lower top line, Kitron will take actions to reduce its cost level and the number of full-time employees in the company.

LACROIX Electronics, the EMS unit of LACROIX Group, generated sales of 42.5 million euros for the Group's fiscal Q2 ended March 31. Sales were 9% below the year-earlier level. For the first six months of fiscal 2013, EMS revenue totaled 81.1 million euros, down 7% year over year. The Group said this drop in first-half revenue, which was expected, should reverse in a buoyant second half through the gradual ramp-up of new business.

Finally, **Connect Group** posted Q1 sales of 30.7 million euros, up 5% sequentially but down 25% year over year. Operating profit (EBIT), including 350,000 euros of reorganization costs, was at break-even. The order book was 78.8 million euros as of March 31, slightly above 77 million euros as of year-end 2012.

Connect Group expects a slight increase in sales and enhanced results in the next quarters due to new customers and the effect of cost savings. However, the company sees the general trend in electronics markets as remaining restrained, and market uncertainty continues to bear down on outlooks.

News

Some new business...**Hon Hai Precision Industry** (New Taipei, Taiwan) is building a low-cost smartphone for **Taiwan Mobile**, Taiwan's number-two mobile carrier, reported *CNA*, the Taiwanese news agency. Also, Hon Hai is producing **Sony's** PlayStation 4 game console, according to a *Digitimes* report….**Flextronics** (Singapore) will expand its existing relationship with **Citrix Systems** (Santa Clara, CA), a cloud computing company, to include manufacturing, fulfillment and repair in Hungary.…*The Wall Street Journal* reported that **Pegatron** (Taipei, Taiwan) will be the main producer of a low-cost iPhone due out later in the year….**Kimball Electronics Group** (Jasper, IN) has received another LED lighting assemblies contract from automotive supplier **Johnson Controls**….**PartnerTech** (Vellinge, Sweden) and **Cavidi** (Uppsala, Sweden), a company in the health and life science sector, have signed a framework agreement for the development of an instrument for HIV tests. …Under a 10-year agreement, **DiaSorin's** Irish branch has selected **Kitron** (Billingstad, Norway) as EMS partner for DiaSorin's nucleic extraction instruments. DiaSorin is an Italian company in the field of in vitro diagnostics….**ESCATEC** (Penang, Malaysia) has helped **Azuri Technologies** (Cambridge, UK) commercialize a solar power charging station designed to provide lighting and mobile phone charging to Africans who lack electricity….**Spektikor** (Oulu, Finland) has contracted **Incap** (Helsinki, Finland) to manufacture electronic subassemblies for a disposable ECG indicator, intended for heart beat monitoring. Also, Incap's India unit has signed a manufacturing agreement with **Tokheim India**. The unit will manufacture PCBAs for Tokheim's fuel retailing equipment.

Adding sheet metal capabilities… **Key Tronic** (Spokane Valley, WA) intends to purchase the assets of **Sabre Manufacturing**, a sheet metal fabricator, for about $5.1 million in cash. With annual revenue of over $7.0 million and about 90 employees, Sabre operates a 66,000-ft^2 facility near the Key Tronic campus in Juarez, Mexico. The acquisition will enable Key Tronic to offer metal fabrication directly to its customers in combination with its other services and will expand its customer base. The deal is expected to close in July and to be immediately accretive to earnings.

Expanding capabilities...**TT electronics integrated manufacturing services**, the EMS subsidiary of TT electronics (Weybridge, UK), is adding the operations of **New Chapel Electronics** (Fairford, UK), a cable harness provider that is already owned by TT electronics. New Chapel supplies interconnect solutions for harsh environments found in the aerospace and defense markets. By integrated New Chapel's operations, TT electronics-IMS will expand its cable and harness capabilities.

Alliances…Under a new alliance with **Mozilla**, Hon Hai is developing more than five devices that run on Mozilla's Firefox mobile operating system, according to published reports….**SigmaTron International** (Elk Grove Village, IL), a publicly held EMS company, and **Infinite Vision** (Scotts Valley, CA), a product development firm, have teamed up for projects where clients need both product development and manufacturing support….EMS providers **Firstronic** (Grand Rapids, MI) and **Maxway Technology** (Shenzhen, China) have formed a joint venture called **Maxtronic** that will be housed initially in Maxway's Shenzhen manufacturing operation. "The new JV gives Firstronic a scalable manufacturing footprint in China and provides Maxway Technology with a partner who can provide similar geographic reach for projects that must be built in the US or Europe," said John Sammut, Firstronic's CEO. Both companies are heavily focused on the automotive market.

New forecasts…A new study from **Frost & Sullivan**, *Analysis of the Indian Electronics Manufacturing Services Market*, predicts that the EMS business in India will grow at a 29% CAGR from $3.79 billion in 2012 to $10.67 billion in 2016. Another Frost & Sullivan study, *EMS Opportunities in the Medical Industry*, finds that EMS revenue from the medical sector totaled more than $16.43 billion in 2012 and estimates that revenue will reach $34.38 billion in 2019. These two values yield a seven-year CAGR of 11%.…**IPC – Association Connecting Electronics Industries** (Bannockburn, IL) has forecasted that the North American EMS market will be worth $69 billion for 2013.

People on the move…**OnCore Manufacturing** (San Jose, CA) has hired Walt Hussey as COO. With over 30 years of manufacturing experience, Hussey held executive operations management positions at OEMs including **Motorola Solutions**, **Symbol Technologies** and **Bose**. He also worked in senior management at both **Sanmina** and **Jabil**….Dag Songedal, managing director of Kitron's Norway operation, has agreed to serve as Kitron's interim CEO. He is replacing Jørgen Bredesen (April, p. 8)….**LACROIX Group** has promoted Vincent Bedouin from managing director of its EMS unit, LACROIX Electronics (Saint-Pierre-Montlimart, France), to managing director of the group. François Beauxis will become managing director of LACROIX Electronics.

Last Word

Do ODMs Pose a Threat to the EMS Industry?

If ODMs are to make a push into the EMS industry, now would be the opportune time. The PC industry, a bread-and-butter source of ODM business, saw shipments drop last year, and volumes are down again in Q1 year over year, giving ODMs that supply the industry a good reason to look for other sources of revenue. Since manufacturing is manufacturing, whether done on an ODM or EMS basis, one could argue that entering the EMS market would be a logical extension for these ODMs. However, *MMI* believes that while ODMs have the requisite manufacturing expertise, they are generally lacking in other areas essential to EMS. Yet ODMs cannot be completely counted out; nor should companies that offer both kinds of services be overlooked.

Most, if not all, large ODMs are Asia-centric manufacturers, with much of their capacity resting in China. By and large, their manufacturing footprints do not accommodate regional manufacturing, a growing requirement in the EMS industry. Even if an ODM had facilities in various regions, that would not be enough to satisfy demand in those regions. A contract manufacturer, whether EMS provider or ODM, must have a fully functioning supply base in each region, presenting ODMs with another barrier to entering the EMS business.

Yet another obstacle faced by ODMs lies in the number of customers that they would have to win and service under an EMS model in order to make a significant impact on sales. ODMs are used to dealing with a relatively small portfolio of customers that doesn't change much. In general, ODMs do not have the business development organizations necessary to pursue a large number of EMS opportunities across multiple markets in different regions. Also, ODMs are not structured to provide account and supply chain management for a much larger client base.

Though ODMs typically lack the organization and distributed footprint to start gobbling up lots of EMS customers across various markets in different countries, their diversification efforts can still pose a threat to some EMS providers. A natural way for an ODM to seek new sources of revenue is to apply its design expertise to more products. Servers have become a product line extension for a number of ODMs looking to diversify. A new product line, such as low-end servers, can attract OEMs that might otherwise design the product and outsource it to an EMS provider. Tablets are another product area targeted by ODMs and at least one EMS provider, **Hon Hai**. Where ODMs and EMS providers set their sights on the same product area, there is the possibility of customers migrating from an EMS solution to an ODM one, especially in the case of commodity-type products.

Though it may be difficult for an ODM to branch out into EMS, there are hybrid companies that already employ both models. **Pegatron** is one such company, and it's becoming a much larger EMS competitor, *MMI* believes, thanks to business awarded by **Apple**. Though Pegatron is not a concern for most EMS providers, it is clearly a competitive threat for Apple's main assembler of handheld devices, Hon Hai. In addition, **Wistron**, another hybrid company, and EMS provider **Jabil** both reportedly produce for **RIM**, which has shrunk its supply base. (Whether the supply base is down to two contractors is unclear.) This month, *Digitimes* reported that Wistron has acquired a RIM R&D activity in Chicago, paving the way for Wistron to serve as ODM for four new BlackBerry smartphones. If this report is accurate, then RIM has shifted away from the EMS model for these new products. Furthermore, Wistron plans to set up a medical unit by the end of the year, according to another *Digitimes* report. Of course, healthcare is a sector coveted by EMS providers.

In *MMI's* opinion, the vast majority of EMS providers have nothing to fear from ODMs that are after additional revenue streams. ODMs generally lack the organization and the footprint necessary to develop and support a broad portfolio of EMS customers. For this reason, the EMS and ODM worlds will remain largely separate. However, the ODM and EMS sectors do overlap for products such as servers, tablets, smart phones and some communications gear, giving OEMs a choice between an EMS and an ODM solution. The two models also intersect within a relatively small number of hybrid companies, which can present a competitive threat, especially for the largest EMS providers.

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