Manufacturing Market ™
INSIDER
inside the contract manufacturing industry
Vol. 21, No. 9 September 2011

EMS Group Continues to Outpace ODMs

In the second quarter, combined year-over-year sales growth of 10 of the largest EMS players continued to surpass by far the aggregate growth of the 10 biggest ODMs. Revenue growth of the EMS group was 24.9 percentage points higher than that of the ODM group (Chart 1, p. 2). The EMS lead in Q2 follows an even bigger winning margin of 34.4 percentage points in the prior quarter (June, p. 3). The ODM sector, whose superior growth in the past was propelled by the PC industry, is now caught in the malaise that has gripped the PC business this year. **IDC**, for one, expects little growth for the PC industry in 2011, as the firm is predicting just a 2.8% increase in PC shipments.

Diversification is finally paying off for the EMS industry in its rivalry with the ODM sector. Benefiting from growth across a number of market segments including non-traditional ones, the group of 10 EMS providers produced a combined growth rate of 24.6% year over year in Q2. For the ODMs, growth was essentially flat at -0.3% (Chart 1). Q2 sales for the EMS group totaled $45.8 billion, compared with $32.5 billion for the ODMs.

Of the EMS group's sales, $27.3 billion, or 60%, came from the colossus, **Hon Hai Precision Industry** (aka Foxconn). With a Q2 growth rate of 32.7% year over year in US dollars, Hon Hai continues to defy the law of large numbers, which says large companies cannot continue adding enough revenue to maintain high growth rates. Hon Hai's 32.7% rate led the entire field of 20 of the largest contract manufacturers. Go figure. Without Hon Hai's contribution, Q2 growth for the EMS group drops to 14.3% year over year, still 9.8 percentage points above what the ODM group was able to attain (Chart 2, p. 2).

Compared with a year earlier, overall sales growth for the 20 CMs in Q2 was 12.9%, 2.6 percentage points below the Q1 rate but still a respectable double-digit result. Besides Hon Hai, only two other CMs – **Cal-Comp Electronics** and **Jabil Circuit** – generated Q2 sales growth of 20% or more, and both are EMS providers. US-dollar sales at six companies declined in Q2 from a year ago, and five of them are ODMs (Table 1, p. 3).

On a sequential basis, the 20 CMs' Q2 sales of $78.3 billion rose by 8.7% from seasonally weak Q1. Six companies turned in sequential increases (in US dollars) of 10% or better, while five CMs saw their sales decrease from the prior quarter.

The 20 CMs together earned net income of approximately $1.2 billion in Q2. Note that this total is imprecise because not all companies follow the same accounting standard. Compared with the prior quarter's total, Q2 net profit was up about 0.8%, well below sales growth of 8.7%. Of the 20 companies, only six achieved a sequential increase in their Q2 net profit.

A year-over-year comparison for aggregate Q2 net profit is even less favorable. Net profit in the quarter was down about 17% versus revenue growth of 12.9%. Just five CMs succeeded in growing their net income from the year-ago quarter (Table 1).

MMI compiled quarterly operating margins for nine out of 10 ODMs. (One ODM, **TPV Technology**, does not report results consistent with those of the other ODMs.) For Q2, overall operating margin for the nine ODMs

Some articles in this issue

Chart 1: Q2 2011 Sales Growth Year Over Year

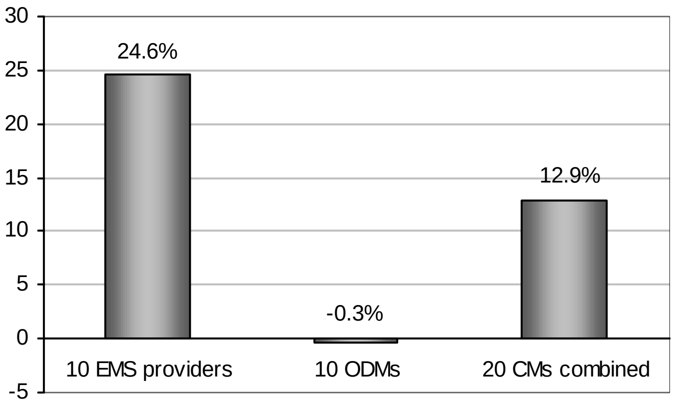
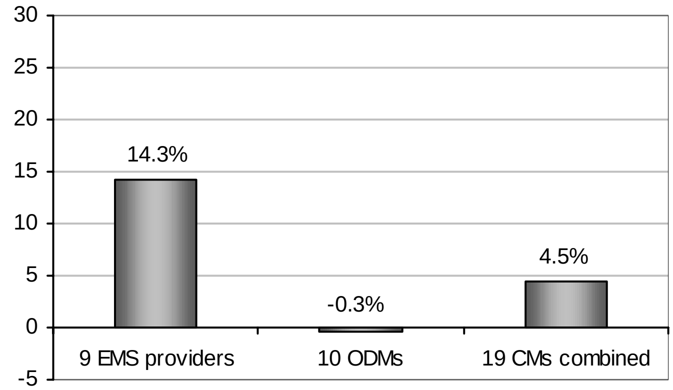


Chart 2: Q2 2011 Sales Growth Year Over Year Excluding Hon Hai



was a paltry 0.87%, down from 1.13% in the prior quarter and down from 1.85% in the year-ago period. By contrast, five large US-traded providers collectively generated an operating margin of 2.8% for Q2 (Aug., p. 2). For the business represented by these ODMs, high operating margins are a thing of the past, at least for now. What's more, the aggregate operating margin for the nine companies has sunk to a barely profitable level that would have been unimaginable a few years ago.

ODM operating margins in Q2 ranged from -1.86% for **Pegatron's** DMS business to 2.18% for **Compal Electronics**. Out of the nine ODMs, Compal was the only one with a Q2 operating margin above 2%.

For the first half, sales of the 20 CMs totaled $150.3 billion, up 14.1% year over year. If this rate held up for the entire year, 2011 would go down as a good year for the contract manufacturing business. However, with headwinds appearing in the US and European economies, odds are increasing that this rate will be eroded by yearend. Also be advised that this double-digit rate owes its existence to Hon Hai. Without Hon Hai, first-half sales growth shrinks to a lackluster 4.3%.

Since sales growth of the EMS group was well ahead of ODM growth in Q1 and Q2, it follows that there would also be a gulf between the two when first-half results were tallied. The first-half growth gap was 29.2 percentage points, based on the EMS group at 28.2% and the ODM group at -1.2% (Chart 3, below). When Hon Hai was omitted, the gap narrowed to a still substantial 16.6% (Chart 4, below).

First-half growth rates varied greatly. Again, Hon Hai achieved the highest revenue growth with a 38.7% increase (in US dollars). Jabil and Cal-Comp also produced growth rates above 20%, consistent with their Q2 performance. **Celestica**, **Flextronics** and **Wistron** were the other companies that accomplished double-digit growth. Eight CMs experienced first-half sales declines or no growth from a year earlier, and seven of them were ODMs (Table 1, p. 3).

For the group of 20 CMs, not only did first-half net income growth fail to keep up with revenue growth, the group's net earnings went in the wrong direction. Combined net profit of approximately $2.5 billion fell by about 19% from the year-earlier period. At fourteen companies, first-half net income (in US dollars) declined from a year earlier.

But net income performance by the EMS side differed greatly from what the ODM group managed to turn in. The EMS group's first-half net in-

Chart 3: First Half 2011 Sales Growth Year Over Year

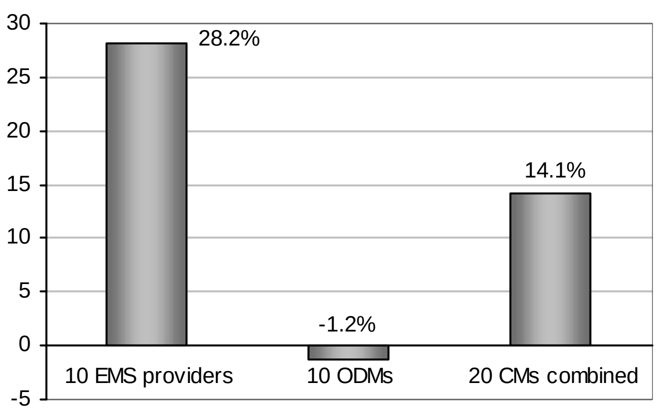
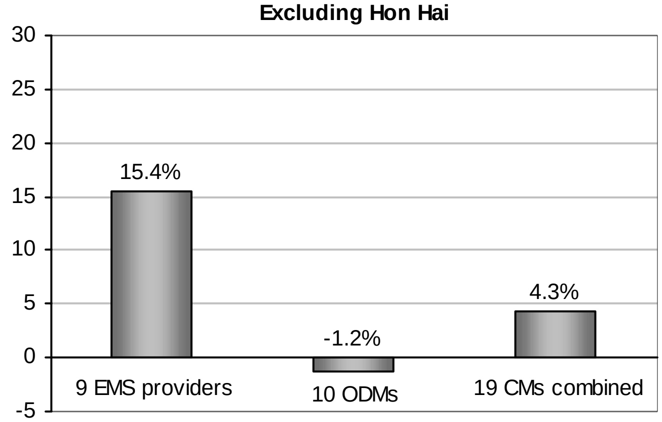


Chart 4: First Half 2011 Sales Growth Year Over Year Excluding Hon Hai



Company (in order of 6-mo. sales)	Primary business	Head-quarters	Reports in US$	Q2 '11 sales	Q1 '11 sales	Qtr.-qtr. chg.	Q2 '10 sales	Yr.-yr. chg.	Q2 '11 net profit	Q1 '11 net profit	Q2 '10 net profit	Q1-2 '11 sales	Q1-2 '10 sales	Yr.-yr. chg.	Q1-2 '11 net profit	Q1-2 '10 net profit
Hon Hai (Foxconn)	EMS	Taiwan	No	27,252	24,895	9.5	20,542	32.7	450	492	526	52,146	37,597	38.7	942	1,090
Quanta Computer	ODM	Taiwan	No	9,514	8,589	10.8	9,267	2.7	186	195	160	18,103	17,181	5.4	381	327
Flextronics	EMS	Singapore	Yes	7,548	6,859	10.0	6,566	15.0	132	135	118	14,407	12,506	15.2	267	178
Compal Electronics	ODM	Taiwan	No	6,115	5,840	4.7	7,132	-14.3	114	119	202	11,955	14,305	-16.4	233	469
Wistron	ODM	Taiwan	No	5,529	4,687	18.0	4,678	18.2	86	69	93	10,216	9,169	11.4	155	178
Jabil Circuit	EMS	Florida	Yes	4,228	3,929	7.6	3,456	22.3	105	55	52	8,156	6,460	26.3	160	82
Pegatron*	ODM	Taiwan	No	3,633	2,923	24.3	3,263	11.3	(24)	(14)	50	6,556	6,716	-2.4	(38)	131
Inventec	ODM	Taiwan	No	3,021	2,847	6.1	2,908	3.9	2	22	36	5,869	5,717	2.7	24	72
TPV Technology	ODM	Taiwan	Yes	2,606	2,691	-3.1	3,063	-14.9	28	42	40	5,297	5,449	-2.8	70	80
Celestica	EMS	Canada	Yes	1,829	1,800	1.6	1,585	15.4	46	30	13	3,630	3,104	16.9	76	42
Sanmina-SCI	EMS	California	Yes	1,674	1,569	6.7	1,625	3.0	7	13	22	3,243	3,153	2.9	20	32
Qisda	ODM	Taiwan	No	1,052	1,107	-5.0	1,006	4.6	4	(40)	28	2,159	2,164	-0.2	(36)	83
Cal-Comp Electronics	EMS	Thailand	No	1,098	1,007	9.0	913	20.3	7	7	17	2,106	1,744	20.8	14	28
Plexus	EMS	Wisconsin	Yes	559	568	-1.6	536	4.3	22	24	24	1,127	1,027	9.7	46	45
Benchmark Electronics	EMS	Texas	Yes	586	538	8.8	589	-0.7	15	15	20	1,124	1,161	-3.2	29	38
Universal Scien-tific Industrial	EMS	Taiwan	No	485	515	-5.9	463	4.8	11	12	17	1,000	917	9.1	23	34
Venture	EMS	Singapore	No	507	460	10.2	469	8.1	34	32	33	968	925	4.6	66	61
AmTRAN Technology	ODM	Taiwan	No	356	528	-32.6	512	-30.4	3	11	16	884	951	-7.0	14	27
Ability Enterprise	ODM	Taiwan	No	370	363	1.8	434	-14.9	6	7	23	733	786	-6.7	14	42
Inventec Appliances	ODM	Taiwan	No	329	285	15.6	357	-7.7	3	2	7	614	688	-10.7	5	8
Total/avg.				**78,292**	**72,001**	**8.7**	**69,366**	**12.9**	**~1,238**	**~1,229**	**~1,498**	**150,294**	**131,719**	**14.1**	**~2,466**	**~3,047**

Table 1: Q2 and Six-Month 2011 Results for Twenty of the Largest Contract Manufacturers (M US$ or %)

Results in non-US currencies were converted to US dollars by applying a three-month average exchange rate for the corresponding quarter. Average exchange rates were based on monthly 2010 and 2011 data from the U.S. Federal Reserve. Net profit totals are approximate because not all companies follow the same accounting standard. *Results correspond to Pegatron's core DMS business.

come, which amounted to approximately $1.6 billion, rose about 0.9% from a year earlier. By contrast, the ODM group's net income of $823 million dropped by about 42% year over year (Table 2, below).

One can rank the top 10 CMs by first-half sales and compare that order to the 2010 standings (May, p. 2). For the first six months of 2011, Hon Hai retained its unassailable position at the top of the order. **Quanta Computer** followed as it did in 2010. But there are changes in the next two positions. Flextronics moved up one step to number three for the first half, replacing Compal, which dropped to fourth place. Fifth through tenth remained the same as last year, the order being **Wistron**, Jabil, Pegatron, **Inventec**, TPV and **Celestica**.

Table 2: Comparing Results Where Companies are Grouped by Primary Business (M US$ or %)

No. of compa-nies	Primary business	Q2 '11 sales	Q1 '11 sales	Qtr.-qtr. chg.	Q2 '10 sales	Yr.-yr. chg.	Q2 '11 net profit	Q1 '11 net profit	Q2 '10 net profit	Q1-2 '11 sales	Q1-2 '10 sales	Yr.-yr. chg.	Q1-2 '11 net profit	Q1-2 '10 net profit
10	EMS	45,766	42,141	8.6	36,745	24.6	~829	~816	~842	87,907	68,594	28.2	~1,644	~1,630
10	ODM	32,526	29,860	8.9	32,621	-0.3	~410	~413	~655	62,387	63,125	-1.2	~823	~1,417
20		78,292	72,001	8.7	69,366	12.9	~1,238	~1,229	~1,498	150,294	131,719	14.1	~2,466	~3,047

Net profit totals are approximate because not all companies follow the same accounting standard.

Hon Hai results for Q2 and the first half

As mentioned previously, Hon Hai's consolidated Q2 sales of $27.3 billion grew 32.7% year over year. In the company's reporting currency, Q2 sales came to NT$785.9 billion, up 20.2%. Note that the disparity in growth rates results from the US dollar's weakening against the NT dollar. On a sequential basis, Q2 sales increased 9.5% in US dollars (7.8% in NT dollars).

Gross margin in Q2 stood at 7.28%, down from 8.11% in the year-ago period and essentially flat versus 7.25% in the prior quarter. Q2 operating margin was 2.01%, down 106 basis points year over year but up 27 basis points sequentially.

Net income in Q2 equaled $450 million, compared with $492 million in the prior quarter and $526 million a year earlier.

For the first half, Hon Hai's consolidated sales totaled $52.1 billion (NT$1,515.2 billion). While sales grew by 38.7% in US dollars (26.4% in NT dollars), net income fell by 13.6% in US dollars (2.5% in NT dollars).

Of that $52.1 billion, **Foxconn International Holdings**, Hon Hai's publicly traded handset subsidiary, accounted for $2.99 billion, or 5.7%. FIH's first-half sales decreased by 7.3% year over year. The handset unit recorded a first-half loss of $17.6 million (attributable to owners of the company), compared with a year-earlier loss of $142.6 million.

Editor's note: This analysis presents a rough approximation of EMS versus ODM sales since a number of the contract manufacturers listed here do both EMS and ODM work. Companies were classified as EMS or ODM based on which model represents their primary business.

News

Hon Hai Expanding into Solar Space

But criticized in an environmental report

Hon Hai Precision Industry (Tucheng City, Taiwan) is making good on its pledge, reportedly made earlier this year, to enter the solar business (June, p. 3). Hon Hai's solar thrust is said to involve two projects, a solar power station in China's Shangxi province and a solar module plant in Jiangsu province.

The megaprovider has inked a memorandum of understanding with **GCL-Poly Energy Holdings**, which describes itself as China's largest polysilicon producer and one of the world's leading solar wafer suppliers. According to published reports, the two companies have partnered to build a 300-megawatt solar power station at Datong in Shangxi province. The project is part of a 200-terawatt program planned by the two companies, *CENS* reported. GCL-Poly is also in the solar power generation business.

Next month, construction is reportedly scheduled to begin for a Hon Hai plant that will turn out solar cells and modules at Funing in Jiangsu province. The total investment there will amount to some $1.5 billion, and capacity will reach 3 gigawatts by 2014, according to two reports.

Hon Hai plans to invest a grand total of $14 billion in its solar efforts including vertically integrated manufacturing, *CENS* reported.

But not all the environment news for Hon Hai is positive. Since 2009, people living near a Hon Hai industrial park in Taiyuan, China, have complained about air emissions from the complex, according to a report on **Apple's** supply chain published last month by five environmental groups. Hon Hai told the *Financial Times* that the complaints are not supported by evidence but that the company is upgrading its air quality systems throughout the plant following a review by local authorities.

SMTC Acquires ZF Array

SMTC (Markham, Ontario, Canada) has acquired **ZF Array Technology**, a privately held EMS provider with operations in San Jose, CA, and Suzhou, China. As SMTC already operates a plant in San Jose, the deal will broaden SMTC's footprint in Silicon Valley and on the West Coast while offering expanded regional capabilities. Through this new acquisition, SMTC will enhance and expand engineering and operational capabilities in prototype development, new product introduction, RF, and burn-in and structural test services.

The purchase price was expected to be about $9.1 million, of which about $2.4 million consists of a two-year earnout based on performance. ZF Array generated revenue of about $27.8 million and EBITDA of about $1.7 million in 2010. Employing 71 people, the company specializes in manufacturing complex electronics equipment and providing systems integration services for telecom, wireless and life science OEMs.

"This transaction is part of SMTC's strategy to grow and diversify its revenue base via accretive acquisitions and is exemplary of our ability to quickly capitalize on attractive acquisition opportunities," stated Alex Walker, co-CEO at SMTC.

The senior management team and employees of ZF will join SMTC, with Bob Zinn, ZF's CEO and majority owner, staying on in an executive advisory and business development capacity.

According to co-CEO Claude Germain, the acquisition of ZF's operations will provide customers with expanded capability in complex RF engineering and systems integration services. "The design, engineering and technical depth of these operations will significantly bolster and differentiate SMTC in San Jose," he said.

SMTC anticipates a one-time expense of about $1.5 million to integrate the two San Jose facilities, which are near each other, and their workforces. Synergies from this combination are expected to yield cost savings of more than $1 million a year, which will kick into full effect by the end of Q4.

In light of this acquisition, SMTC now expects to produce EBITDA of about $3 million (excluding deal costs) in Q4.

Hunter to Add Spinnaker Microwave

Hunter Technology, a Santa Clara, CA-based EMS provider with a PCB fabrication capability, has signed an agreement to acquire **Spinnaker Microwave**, a provider of RF and microwave solutions that is also based in Santa Clara. According to Hunter, the acquisition creates one of the EMS industry's strongest RF solutions providers. Terms of the deal were not disclosed.

Spinnaker's solutions include signal source components and integrated subassemblies used in defense, scientific, and test and measurement applications. The company specializes in customer collaboration on the design and development of integrated RF solutions up through 50 GHz including frequency synthesizers, microwave receivers, up/down converters and MM-wave subsystems that are not available as off-the-shelf products.

"The addition of RF/microwave engineering products and development capabilities further extends Hunter's reach into the front-end of the product development cycle. Spinnaker's enhanced test expertise also extends our back-end capabilities as we accelerate our maturation into high-level assemblies and systems enabling us to bring significantly more value to our customers," said Joseph O'Neil, chairman, president and CEO of Hunter.

After the deal is closed, Spinnaker will become a wholly owned subsidiary of Hunter, which presents itself as a provider of EMS to industry leaders in the defense, aerospace, test and measurement, and medical markets. Hunter already has RF expertise in the fabrication, assembly and test of complex microwave circuitry.

EMS Deal in Northeast US

Da-Tech, an EMS company located in Ivyland, PA, has bought assets of another EMS provider, **Synchronized Manufacturing Technologies** of Salem, NH. The purchase price was not disclosed.

"The reputation of being a high-quality electronic contract manufacturer in the Northeast was a major factor in acquiring Synchronized Manufacturing Technologies. We believe it is an excellent fit for all parties, especially for the existing customer base that Synchronized has," stated Paul Litwack, CEO of Da-Tech.

But Synchronized ceased operations this month, and Da-Tech will not be taking over the New Hampshire facility, reported *New Hampshire Business Review*. An auction of facility equipment is scheduled to take place this month.

Founded in 1975, Da-Tech is a private, full-service contract manufacturer working from design through to final shipment. Markets served by Da-Tech consist of avionics, aerospace, medical equipment, communications systems and precision industrial controls.

*Alliance…***Season Group** (Hong Kong), a vertically integrated EMS provider with facilities in Asia and North America, has signed a memorandum of understanding with a British EMS provider, **Outsource Electronics Limited** (Havant, UK). Through this prospective alliance, Season can now offer an enhanced global service to its UK customers. The partnership will also allow Season's international customers to take advantage of local UK manufacture and aftermarket services previously unavailable to them. Outsource Electronics believes that this relationship with Season will benefit a number of its current customers as well as attract new business from clients that require the services of both companies.

*Some new business…*Hon Hai has begun manufacturing Ultrabooks for **HP** and will handle production of 10.1-in. tablets for **Amazon**, according to reports by Taiwan's *Digitimes.* …**Flextronics** (Singapore) has expanded its relationship with **Lockheed Martin** beyond PCB assembly to full system-level integration. Flextronics will now support full system manufacturing and aftermarket services for a range of Lockheed Martin's aerospace and defense products from Flextronics' Plano, Texas, facility. Also, **Sonus Networks**, an IP networking company, has selected Flextronics as its end-to-end manufacturing partner for production, order fulfillment, new product development and post-manufacturing logistics services. This contract covers all of Sonus' products.…**RedFlow** (Brisbane, Australia), an electricity storage system company, recently chose **Jabil Circuit** (St. Petersburg, FL) to serve as the outsourced manufacturing partner for RedFlow's zinc-bromine battery modules (ZBMs). The contract with Jabil is an acceleration of RedFlow's expansion plans. Jabil will initially manufacture ZBM components as its plastics plant in Taichung, Taiwan. As of June, Jabil was separately negotiating with RedFlow to integrate ZBMs for products in the telecom market. In addition, Jabil will manufacture a solder paste inspection system for **ORPRO Vision**….**Kaiam** (Newark, CA) has selected **Sanmina-SCI** (San Jose, CA) to industrialize and manufacture a family of optical components using Kaiam's MEMS-based hybrid integration technology. The new products will be ramped to full production in Sanmina-SCI's facilities in Shenzhen, China….France's **Hager Group** recently contracted **Videoton** (Székesfehérvár, Hungary) to manufacture smart building automation products. Also, Videoton's battery pack assembly operation in Marcali, Hungary, has landed another customer from Japan, **FDK**….**Redline Communications**, a developer of wireless broadband products, has awarded SMTC a contract to manufacture Redline's RDL-3000, a next-generation, broadband wireless radio. Since 2009, SMTC has manufactured Redline's AN-80i broadband wireless radio in Chihuahua, Mexico….**CTS Electronics Manufacturing Solutions** (Lisle, IL) has announced two new programs to provide PCB and high-level assemblies. A firm in the scientific analysis business awarded the first program, whose revenue is expected to reach about $11 million in 2012. The second one, which supports a new type of instrument used in orthopedic surgery, starts at about $3 million in revenue next year and grows to about $14 million in 2013….**Lighting Science Group** (Satellite Beach, FL), an LED lighting company, has partnered with EMS provider **Dixon Technologies**, based in Noida, India, to jointly manufacture and distribute LED lighting products. Utilizing Dixon's manufacturing facilities in Noida will enable Lighting Science to meet the expected strong demand for LED lighting products in India….**BAE Systems Manufacturing** (Hillend, Fife, UK) has received a contract from **SELEX Galileo** to provide procurement and EMS for a radar system that is the primary sensor for the Typhoon jet. The order is worth over £20 million….**IEC Electronics** (Newark, NY) recently secured an order valued at more than $5.2 million from a top 10 prime defense contractor. This award calls for providing ground support equipment and unique flight systems cables and wire harnesses….The EMS/SenDEC division of **API Technologies** (Orlando, FL) has landed orders totaling $3.6 million to produce circuit card assemblies for use in IED (improvised explosive device) jamming and electronic warfare systems. These orders came from two global defense firms. In addition, the division recently gained contracts with an aggregate value of $2.7 million to supply circuit card assemblies for use in counter-explosive equipment under the Joint Counter Radio-Controlled Improvised Explosive Device Electronic Warfare (JCREW) program. A major integrator of defense electronics systems awarded the contracts.

*Solar business lost…*In July, **Day4 Energy** (Burnaby, BC, Canada) decided to cease outsourced production at Jabil in Poland and started negotiations for terminating the manufacturing contract. Day4 is transforming its business from PV (photovoltaic) module manufacturing and distribution to a technology and brand licensing model. Day4 will now obtain all of its PV module output from licensees.

German EMS Providers Investing in N. America

North America continues to attract investment from EMS providers based outside the region (Oct. 2010, p. 1-3). Two German EMS providers, one an established name and the other a new player, are in different stages of pursuing the North American market.

Zollner Elektronik (Zandt, Germany) plans to expand in the US market by establishing a full-service NPI center in Milpitas, CA. The Silicon Valley facility, which will include low- to medium-volume manufacturing capabilities, will complement Zollner's Northern Virginia resources and its alliance with **EIT**, formed in 2009.

The NPI center is designed to better serve customers throughout North America and support Zollner's European and Asian production facilities. Including low- to medium-volume production capabilities to meet regional and domestic requirements will broaden Zollner's portfolio of services for OEMs based in North America.

With the center, Zollner will gain enhanced coverage of customers with an emphasis on improving technical support and shortening time-to-market for new product introductions.

Then there's the new player, **Limtronik** (Limburg, Germany). The EMS provider's new manufacturing facility is going up in the metropolitan area of Denver, CO. Having decided to offer its manufacturing services in North America, the EMS provider established a subsidiary, Limtronik USA, for the region last year. Then in May 2011, the company engaged a process manager with EMS experience to build the subsidiary into a manufacturing base in North America. Limtronik has at least one customer for the new facility, a well-known client.

Formerly the Limburg site of **EN ElectronicNetwork**, Limtronik emerged as an independent provider in 2010 when EN ElectronicNetwork divested the site.

*More facility projects…*Hon Hai plans to set up a manufacturing base in Malaysia, according to published reports from Taiwan. Construction has begun on an industrial campus in Kulai City, reported *CNA*. The company intends to make printer cartridges and mobile phone cases in Malaysia, wrote *CENS*, citing local news sources. *CENS* also reported that Hon Hai has decided to invest NT$100 billion ($2.4 billion) in building an automation complex in Taichung, Taiwan, for the production of such things as machine tools, automation equipment and robots. Hon Hai recently made a big splash when it reportedly said it intends to employ 300,000 robots next year and 1 million robots in three years….**Kitron** (Billingstad, Norway) has officially opened its Ningbo, China, factory, its first site in Asia. This move is based on a strategy to offer EMS to existing and new customers in the Asian markets and to provide competitive manufacturing services to Kitron's operations in Europe....**OnCore Manufacturing Services** (San Jose, CA) has opened a new product introduction and manufacturing facility in Wilmington, MA. The facility will provide medical, aerospace and defense, and industrial customers with a broader range of product commercialization services….**Dynamic Manufacturing** (Freeport, PA), a **Matric Group** company, recently broke ground for an expansion project that will double its manufacturing space from 10,000 ft^2 to 20,000 ft^2. The project will bring Dynamic's facility to a total of 24,000 ft^2, including administrative offices….**Legacy Electronics** (Sioux Falls, SD), a contract manufacturer, designer and tester of memory modules, PCBs and other computer products, has begun production at its 40,000-ft^2 plant in Canton, SD. In June, the company completed the first phase of its move from San Clemente, CA….EMS provider **Custom Interconnect Ltd** of Andover, UK, has taken possession of a product manufacturing facility with 10,000 ft^2 of additional space in Andover.

Elcoteq Units File for Bankruptcy

Elcoteq Network, the subsidiary of **Elcoteq** in charge of its material purchases and customer invoicing in Europe, has filed for bankruptcy. Since Elcoteq Network's payment transactions have been blocked as a result of credit facility lenders' continued enforcement actions, the subsidiary is no longer able to continue its activities. Elcoteq was unable to repay 48.5 million euros owned on its revolving credit facility, which expired on June 30. (See also July, p. 1; Aug., p. 8.)

In addition, Elcoteq's three Finnish subsidiaries have filed for bankruptcy due to lack of funding of those companies brought about by the lenders' enforcement actions. This filing affects about 100 employees in Finland. Elcoteq, the parent company, continues the controlled management process under the laws of Luxembourg, where it is domiciled.

In August, Elcoteq announced that **Platinum Equity**, which had considered making a major equity and debt investment in Elcoteq, decided against investing in the company.

Elcoteq's Q2 sales of 175.7 million euros declined by 47% year over year and 8% quarter on quarter. The sequential sales decline resulted from existing customers being cautious in their outsourcing to Elcoteq as the customers were concerned about the company's financial situation. Due to the situation, it was also extremely difficult to make new customer deals during the second quarter.

The company posted a Q2 operating loss of 37.8 million euros versus a Q1 loss of 11.1 million euros and recorded a Q2 net loss to equity holders of 63.7 million euros compared with a Q1 net loss of 20.4 million euros. Excluding one-time write-downs, the Q2 operating loss would have been 11.7 million euros.

On Aug. 31, Elcoteq reported that it did not have adequate financing available then to run its operations in the future and therefore will no longer prepare its financial statements on a going-concern basis. The company said it has no visibility with regard to the outlook for the rest of the year due to the actions taken by its lenders and the reactions of suppliers and customers. Elcoteq also noted that it is possible that customers and other stakeholders may lodge various claims against the company, but the monetary impact of these potential claims cannot be estimated.

Elcoteq has asked the Finnish National Bureau of Investigation to establish whether the revolving credit facility lenders or their representatives have committed gross usury or other criminal acts against the company in connection with the revolving credit facility agreement signed in November 2009.

Closures...Flextronics plans to close its plant in Skive, Denmark, reported *Skive Folkeblad*, a local newspaper. An ex-Flextronics employee is trying to start a new EMS business nearby, the paper said….**Benchmark Electronics** (Angleton, TX) intends to shutter its Dublin, Ireland, facility by the end of this year….This month, an equipment auction is scheduled to take place in connection with the closure of **Millennium Electronics'** EMS facility in Crystal Lake, IL, according to the website of **The Branford Group**, an auction company.....**Scanfil EMS** (Sievi, Finland) aims to close its plant in Vantaa, Finland. Plans are to move the majority of the plant's production to the provider's factories in China and part of it to another Scanfil plant in Finland.

People on the move...**Venture** (Singapore) has appointed Tan Kian Seng as president. He has been a member of Venture's senior management team since joining the group in 2001 and has served as CFO since 2006. With this change, CEO Wong Ngit Liong will devote more time to focus on new business growth opportunities and building new capabilities in the group….OnCore Manufacturing has promoted Sajjad Malik to the newly created position of COO.

Pairing Growth with Higher Margins

In the past, high growth and healthy margins were often mutually exclusive. A provider could grow quickly, but landing business at high win rates meant that margins would be sacrificed in many cases. Dropping margins to win business is not as great a temptation when the EMS industry is growing at double digits as it has been through 2010 and the first half of 2011. But as last month's cover story shows, a slowdown in the EMS space may be in the works. If, indeed, the US and Europe are "dangerously close to recession," as **Morgan Stanley** is now saying, then EMS providers will feel more pressure to win business in order to compensate for persistently weak demand. Does this mean that the old margin-dropping strategy will again rear its slimy head?

Not necessarily. EMS providers, most notably three of the largest ones, are placing more and more emphasis on business that combines above average growth with higher margins. *MMI* believes that this relatively new strategy will give companies a powerful weapon for fighting off the economic doldrums in the US and Europe.

Jabil Circuit, an early adopter of this strategy, is perhaps its poster child. In the Jabil version of the strategy, the company has lumped a number of areas into its Diversified Manufacturing Services segment, expected to exhibit a long-term growth rate of 20% to 30% and non-GAAP operating margins above the corporate average. The company will increasingly rely on this segment to fuel its growth, and the segment is getting more than its fair share of investment. Jabil's goal is to derive half of its business from this segment.

Flextronics has also changed its revenue breakdown by transforming five market segments into four business groups. The two groups with the highest non-GAAP operating margin profiles, High Reliability Solutions and Industrial & Emerging Industries, also have the highest projected growth rates (15%-20%) over the long term. As part of this makeover, Flextronics is pulling out of the PC ODM business, where market growth and margins had declined.

Then there's **Celestica**. The provider groups industrial, aerospace and defense, healthcare and green technology business into a diversified end markets segment. Celestica's goal is to raise the segment's share of total sales from 13% to 25% to 30% over the next three years. That means the segment's growth will be well above the company's average. Now Celestica hasn't talked about its expectations for the segment's margins, but it is well known that the businesses within the segment can potentially command higher margins than other sectors served by the EMS industry.

The shift toward higher margin, higher growth business is not just a matter of focusing on low-volume, high-mix business in the non-traditional segments. Providers are also seeking out new markets in such areas as clean tech, aftermarket services, healthcare, mechatronics and industrial equipment.

This is a major development within the EMS industry. And it couldn't have come at a better time.

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Manufacturing Market Insider is a monthly newsletter published by JBT Communications, 43 Summit Ridge, Burlington, VT 05401-3911. Phone (802) 651-9334. Fax (802) 651-9336.

ISSN 1072-8651

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