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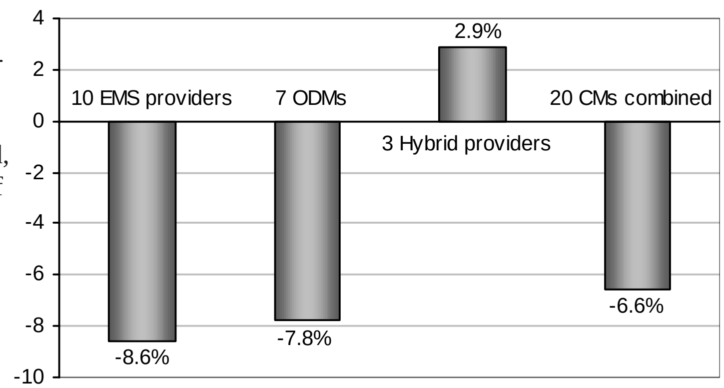
# First-Half Growth Favors Hybrid Providers

Based on first-half results of 20 of the largest contract manufacturers, neither the EMS approach nor the ODM model has enjoyed an appreciable advantage this year so far. Combined first-half sales of 10 large EMS providers fell at nearly the same year-on-year rate as the aggregate sales of seven large ODMs. Revenue for the EMS group dropped 8.6%, while the ODMs' sales sank 7.8%. Apparently, both groups were buffeted almost equally by the macroeconomic headwinds swirling about the global economy. But that is not the end of the story of the first six months.

There is a third class of contract manufacturers – the hybrid provider that does substantial amounts of both EMS and ODM business. In contrast with the declines of the EMS and ODM groups, combined sales of three large hybrid CMs actually grew in the first half. The hybrid group's revenue increased 2.9% year over year, more than 10 percentage points better than the performance of the other two groups (Chart 1). If this comparison can be generalized, it would seem that the hybrid model did a better job of withstanding the vicissitudes of the first half.

Though providing EMS and ODM services within the same company is not a new idea, in the past *MMI* did not single out the hybrid class of CMs. They were treated as EMS providers or ODMs depending on which side of the business supplied the majority of sales. What has changed? In a word, **Pegatron**. Spun off from **Asustek** in 2010, Pegatron has emerged as one of the world's largest contract manufacturers, having risen to second biggest in terms of total first-half revenue (see Table 1, p. 2) or number three if you just count Pegatron's core DMS revenue of $13.0 billion for the first half. While Pegatron is known as an ODM, much of its recent growth has been fueled by its **Apple** assembly business, which has expanded the EMS piece of Pegatron's revenue pie. Reportedly, Pegatron has built iPad Mini tablets and some versions of the iPhone for Apple.

**Chart 1: First-Half Growth Year on Year**




**Wistron** is another large player operating as both an ODM and an EMS provider. Although the company has a reputation of being a major notebook ODM, Wistron has a history of doing business on both sides of the outsourcing street. Most recently, unconfirmed reports say that Wistron will join Apple's supply chain.

The third and final company placed in the hybrid group is **Venture**, an EMS provider that has built up an ODM business. In 2012, Venture's ODM business accounted for about

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| Company (in order of 6-mo. sales) | Primary business | Head-quarters | Reports in US$ | Q2 '13 sales | Q1 '13 sales | Qtr.-qtr. chg. | Q2 '12 sales | Yr.-yr. chg. | Q2 '13 net profit | Q1 '13 net profit | Q2 '12 net profit | Q1-2 '13 sales | Q1-2 '12 sales | Yr.-yr. chg. | Q1-2 '13 net profit | Q1-2 '12 net profit |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Hon Hai (Foxconn) | EMS | Taiwan | No | 30,010 | 27,431 | 9.4 | 30,127 | -0.4 | 569 | 554 | 407 | 57,442 | 63,863 | -10.1 | 1,123 | 943 |
| Pegatron | ODM/EMS | Taiwan | No | 7,111 | 7,378 | -3.6 | 7,408 | -4.0 | 47 | 78 | 65 | 14,489[1] | 13,202 | 9.8 | 125 | 67 |
| Quanta Computer | ODM | Taiwan | No | 6,400 | 6,697 | -4.4 | 8,130 | -21.3 | 135 | 151 | 202 | 13,097 | 16,128 | -18.8 | 286 | 375 |
| Compal Electronics[2] | ODM | Taiwan | No | 5,592 | 5,681 | -1.6 | 5,570 | 0.4 | 47 | 46 | 55 | 11,273 | 11,020 | 2.3 | 93 | 119 |
| Flextronics | EMS | Singapore | Yes | 5,791 | 5,295 | 9.4 | 5,976 | -3.1 | 59 | (49) | 137 | 11,086 | 12,346 | -10.2 | 10 | 280 |
| Wistron | ODM/EMS | Taiwan | No | 5,460 | 5,364 | 1.8 | 5,369 | 1.7 | 58 | 55 | 70 | 10,824 | 11,329 | -4.5 | 113 | 127 |
| Jabil[3] | EMS | Florida | Yes | 4,468 | 4,417 | 1.1 | 4,251 | 5.1 | 50 | 89 | 101 | 8,885 | 8,487 | 4.7 | 139 | 199 |
| Inventec | ODM | Taiwan | No | 3,459 | 3,417 | 1.2 | 3,399 | 1.8 | 54 | 60 | 47 | 6,876 | 6,850 | 0.4 | 114 | 62 |
| Sanmina | EMS | California | Yes | 1,489 | 1,428 | 4.3 | 1,549 | -3.9 | 19 | 21 | 9 | 2,917 | 3,012 | -3.2 | 40 | 8 |
| Celestica | EMS | Canada | Yes | 1,495 | 1,372 | 8.9 | 1,745 | -14.3 | 28 | 11 | 24 | 2,868 | 3,436 | -16.5 | 39 | 67 |
| Cal-Comp Electronics[4] | EMS | Thailand | No | 1,015 | 994 | 2.2 | 1,220 | -16.8 | 8 | 9 | 13 | 2,009 | 2,321 | -13.4 | 17 | 20 |
| Qisda | ODM | Taiwan | No | 982 | 933 | 5.3 | 941 | 4.4 | 19 | (29) | (33) | 1,915[5] | 1,925 | -0.5 | (9) | (17) |
| Shenzhen Kaifa Technology | EMS | China | No | 606 | 595 | 1.9 | 693 | -12.5 | 9 | 5 | 3 | 1,201 | 1,333 | -9.9 | 14 | 10 |
| Benchmark Electronics | EMS | Texas | Yes | 608 | 542 | 12.0 | 630 | -3.6 | 9 | 12 | 14 | 1,150 | 1,223 | -6.0 | 20 | 19 |
| Plexus | EMS | Wisconsin | Yes | 572 | 558 | 2.5 | 609 | -6.1 | 23 | 18 | 24 | 1,130 | 1,182 | -4.4 | 41 | 44 |
| Universal Scien-tific Industrial | EMS | China | No | 475 | 556 | -14.4 | 453 | 5.0 | 15 | 21 | 15 | 1,031 | 918 | 12.2 | 36 | 31 |
| Venture | EMS/ODM | Singapore | No | 471 | 429 | 9.8 | 484 | -2.8 | 24 | 23 | 27 | 899 | 939 | -4.2 | 47 | 55 |
| Kinpo Electronics[4] | ODM | Taiwan | No | 435 | 393 | 10.6 | 288 | 51.1 | 7 | 10 | 5 | 829 | 503 | 64.6 | 17 | (1) |
| Ability Enterprise | ODM | Taiwan | No | 221 | 240 | -7.7 | 398 | -44.4 | 4 | 3 | 13 | 461 | 736 | -37.4 | 7 | 24 |
| AmTRAN Technology | ODM | Taiwan | No | 227 | 218 | 4.2 | 338 | -32.9 | 9 | 8 | 15 | 445 | 692 | -35.7 | 18 | 30 |
| **Total/avg.** | | | | **76,889** | **73,938** | **4.0** | **79,576** | **-3.4** | **~1,192** | **~1,096** | **~1,212** | **150,826** | **161,445** | **-6.6** | **~2,288** | **~2,462** |
| **Total/avg. without Hon Hai** | | | | **46,878** | **46,506** | **0.8** | **49,449** | **-5.2** | **~623** | **~541** | **~805** | **93,384** | **97,582** | **-4.3** | **~1,165** | **~1,519** |

**Table 1: Q2 and Six-Month 2013 Results for 20 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 2012 and 2013 data from the US Federal Reserve. Company net profits shown here are attributable to shareholders. Net profit totals are approximate because not all companies follow the same accounting standard. [1] DMS revenue accounted for 89.7% of Pegatron's six-month sales shown here. DMS sales were not presented because Pegatron stopped reporting DMS net income. [2] A member of the Kinpo Group. [3] For Jabil, Q2 '13 corresponds to the quarter ended May 31. [4] A member of the New Kinpo Group, a subgroup under the Kinpo Group. [5] DMS business accounted for 67.5% of Qisda's six-month sales shown here.

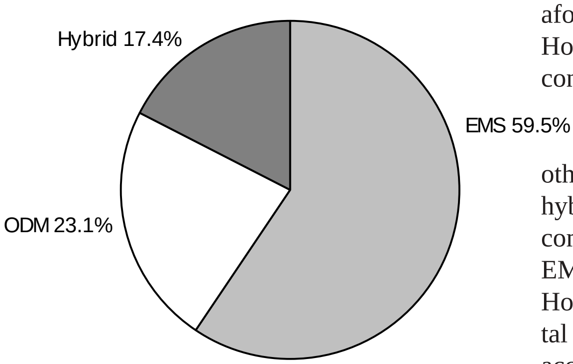
35% of the company's sales. Other companies among the 20 CMs may deserve to be considered hybrid providers, but these are the three that *MMI* has identified so far as having established substantial businesses of both types.

By first-half revenue, the hybrid providers comprise the smallest of the three groups into which the 20 CMs are divided. Sales of the hybrid CMs totaled $26.2 billion, or 17.4% of the combined sales of the group of 20. By far the largest share of total sales – 59.5% – belonged to the EMS group, while the ODMs generated 23.1% (Chart 2, p. 3).

First-half sales of the 20 CMs amounted to $150.8 billion, down 6.6% year over year. *MMI* believes that this figure can be used as a proxy for the board- and system-level outsourcing space, since these 20 companies account for the vast majority of revenue from the space. **Hon Hai Precision Industry**, the EMS giant, did not influence this result in a big way. Without Hon Hai, the drop would have been 4.3%.

Of the 20 CMs, 14 experienced first-half sales declines in US dollars ranging from slight to rather severe. Seven companies endured double-digit

Chart 2: First-Half Sales by Provider Type




decreases, with ODMs **Ability Enterprise** and **AmTRAN Technology** suffering declines of over 30% (in US dollars) from a year earlier. Of the six CMs that raised their first-half sales versus a year ago, just two – **Universal Scientific Industrial** and **Kinpo Electronics** – achieved double digit growth (Table 1, p. 2). Kinpo Electronics separated itself from the other CMs with a 64.6% gain.

For the first six months, the 20 CMs together earned net income of approximately $2.29 billion. (Net income was approximate because not all companies follow the same accounting rules.) Net profit was down about 7.1% year on year, in line with the aforementioned sales decline of 6.6%. However, unlike the EMS and ODM contingents, the hybrid group improved its net income from a year earlier (Table 2 below). On the other hand, first-half net margin for the hybrid group came in at about 1.1%, compared with about 1.6% for the EMS group and 1.5% for the ODMs. Hon Hai contributed some 49% of total net income for the first half, while accounting for 38% of sales.

Second-quarter revenue for the entire group totaled $76.9 billion, up 4.0% from the prior quarter but down 3.4% from the year-ago period. Sequential increases on the part of 15 CMs outweighed declines produced by the others. Two companies, **Benchmark Electronics** and Kinpo Electronics, sported double-digit gains. Excluding Hon Hai, sequential growth in Q2 was a barely positive 0.8%.

In the year-on-year comparison, Q2 decreases from 13 companies more than offset increases by seven CMs. Six CMs faced two-digit drops in their revenue (expressed in US dollars), with Ability and AmTRAN showing the worst declines (Table 1). Again, Kinpo Electronics stood out with its 51.5% growth in Q2.

The EMS and hybrid groups had nearly identical sales declines from the year-earlier quarter. In Q2, the EMS group's revenue fell 1.5%, while the hybrid group's revenue dropped 1.6%. By contrast, Q2 sales of the ODM group decreased 9.2%. When compared with the prior quarter, the EMS group's sales rose 7.7%, a far better result than the 1.5% drop of the ODM group or the 1.0% decline of the hybrid group (Table 2).

Q2 net income for the group of 20 was approximately $1.19 billion, up from about $1.10 billion in the previous quarter but down from about $1.21 billion a year earlier. Net income fell about 1.7% year over year, a slightly better outcome than the Q2 sales decline of 3.4%. Eight CMs boosted their net income from a year ago, but this combined effort was not enough to counter the declines at the other providers. Without Hon Hai, the drop in Q2 net income would have been much worse – about 22.6% year on year instead of about 1.7%.

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

| No. of companies | Primary business | Q2 '13 sales | Q1 '13 sales | Qtr.-qtr. chg. | Q2 '12 sales | Yr.-yr. chg. | Q2 '13 net profit | Q1 '13 net profit | Q2 '12 net profit | Q1-2 '13 sales | Q1-2 '12 sales | Yr.-yr. chg. | Q1-2 '13 net profit | Q1-2 '12 net profit |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 10 | EMS | 46,530 | 43,188 | 7.7 | 47,252 | -1.5 | ~789 | ~690 | ~746 | 89,718 | 98,122 | -8.6 | ~1,479 | ~1,621 |
| 7 | ODM | 17,317 | 17,579 | -1.5 | 19,063 | -9.2 | ~275 | ~250 | ~305 | 34,896 | 37,854 | -7.8 | ~525 | ~593 |
| 3 | ODM/EMS | 13,042 | 13,170 | -1.0 | 13,261 | -1.6 | ~129 | ~156 | ~162 | 26,212 | 25,469 | 2.9 | ~285 | ~249 |
| 20 | | 76,889 | 73,938 | 4.0 | 79,576 | -3.4 | ~1,192 | ~1,096 | ~1,212 | 150,826 | 161,445 | -6.6 | ~2,288 | ~2,462 |

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

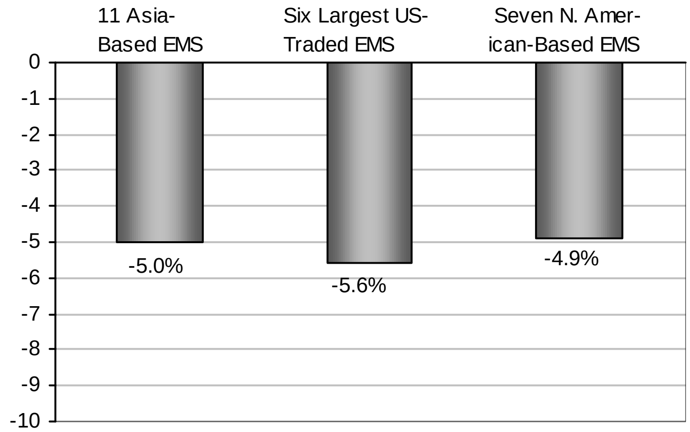
# First-Half Decline for Asian Group

A group of 11 large and mid-sized EMS providers based in Asia produced a first-half sales decline that nearly mirrored the declines of two other industry groups tracked by *MMI*. First-half 2013 sales of the Asia-based group fell 5.0% year on year, compared with an combined 5.6% drop for the six largest US-traded EMS providers and a 4.9% decrease for a group of seven mid-tier and smaller providers based in North America (Chart 1A, p. 4) ). With respect to first-half sales, Asia-centric manufacturing did not prove to be an overall advantage for the Asian group. Nor, for that matter, did Asia-based production become a drawback in light of a growing trend toward onshoring (keeping new programs in higher-cost geographies) and reshoring (relocating work from lower-cost to higher-cost regions). Indeed, it appears that a weak demand environment had virtually the same effect on each of the three industry groups in the publicly traded sector. Note that all of the EMS providers in this comparison are publicly listed or are part of a publicly traded company.

First-half revenue for the 11 Asia-based providers totaled $6.69 billion, down from $7.04 billion in the year-ago period. For the first six months, declines at six EMS providers outweighed growth at five others. Three players – **Cal-Comp Electronics**, **Pan-International Industrial** and **PCI** – chalked up double-digit declines (in US dollars). On the other hand, three other providers – **Universal Scientific Industrial**, **Fabrinet** and the OEM Manufacturing Division of **WKK International (Holdings)** – grew their revenue by two-digit percentages (Table 1A below).

Two of the 11 Asian providers, WKK and **Wong's International Holdings**, report results only a half-year basis. For the remaining nine players, sales for Q2 2013 amounted to $3.14 billion, up 1.6% sequentially but down 8.5% year over year. All but one of the nine providers increased their sales from the prior quarter, and four of these – **Integrated Micro-Electronics Inc.**, Pan-International, **SVI** and PCI – achieved double-digit gains. But in the year-over-year comparison, six out of nine providers saw their sales drop, and three companies – Cal-Comp, **Shenzhen Kaifa Technology** and PCI – faced double-digit declines (Table 1A).

**Chart 1A: First-Half Growth Year on Year**




In Q2, the nine providers together earned net income of approximately $81 million for a net margin of about 2.6%. (Net income was approximate because not all companies follow the same accounting rules.) The highest net margins in the quarter were turned in by SVI at 10.1% and **Fabrinet** at 9.4%. Collectively, net income fell about 9% sequentially despite 1.6% growth in sales from the prior quarter. Sequential net income declines at five companies more than offset gains at four others.

But on a year-over-year basis, combined Q2 net income for the nine companies grew, though sales declined.

**Table 1A: Six-Month 2013 Results for 11 Asia-Based EMS Providers (M US$ or %)**

| Company | Head-quarters | Reports in US$ | Q2 '13 sales | Q1 '13 sales | Qtr.-qtr. chg. | Q2 '12 sales | Yr.-yr. chg. | Q2 '13 net profit | Q1 '13 net profit | Q2 '12 net profit | Q1-2 '13 sales | Q1-2 '12 sales | Yr.-yr. chg. | Q1-2 '13 net profit | Q1-2 '12 net profit |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| Cal-Comp Electronics | Thailand | No | 1,015 | 994 | 2.2 | 1,220 | -16.8 | 7.6 | 9.2 | 12.9 | 2,009 | 2,321 | -13.4 | 16.8 | 20.5 |
| Shenzhen Kaifa Technology | China | No | 606 | 595 | 1.9 | 693 | -12.5 | 8.9 | 5.2 | 3.2 | 1,201 | 1,333 | -9.9 | 14.2 | 10.5 |
| Universal Scientific Industrial | China | No | 475 | 556 | -14.4 | 453 | 5.0 | 15.3 | 20.8 | 14.8 | 1,031 | 918 | 12.2 | 36.1 | 31.1 |
| Venture | Singapore | No | 471 | 429 | 9.8 | 484 | -2.8 | 24.1 | 22.6 | 26.6 | 899 | 939 | -4.2 | 46.7 | 54.7 |
| Integrated Micro-Electronics Inc. | Philippines | Yes | 186 | 165 | 12.7 | 174 | 6.9 | 1.8 | 0.3 | 2.3 | 351 | 326 | 7.6 | 2.1 | 3.1 |
| Fabrinet | Thailand | Yes | 160 | 156 | 2.8 | 143 | 12.0 | 15.1 | 21.1 | 7.5 | 316 | 282 | 12.0 | 36.2 | (38.8) |
| Pan-International Industrial | Taiwan | No | 118 | 101 | 17.2 | 130 | -8.9 | 1.5 | 1.9 | 1.5 | 220 | 267 | -17.7 | 3.3 | 2.8 |
| SVI | Thailand | No | 63 | 54 | 16.1 | 66 | -5.3 | 6.3 | 7.5 | 4.9 | 117 | 118 | -0.7 | 13.8 | 14.7 |
| PCI | Singapore | Yes | 45 | 41 | 11.6 | 70 | -35.1 | 0.3 | 0.2 | 2.6 | 86 | 125 | -31.1 | 0.5 | 5.1 |
| **Subtotal/avg.** | | | **3,139** | **3,089** | **1.6** | **3,432** | **-8.5** | **~81** | **~89** | **~76** | **6,228** | **6,627** | **-6.0** | **~170** | **~104** |
| WKK International (Holdings) | Hong Kong | No | | | | | | | | | 241 [1] | 201 [1] | 20.0 | 3.3 [2] | 2.2 [2] |
| Wong's International Holdings | Hong Kong | No | | | | | | | | | 219 | 210 | 4.2 | 3.7 | 3.7 |
| **Six-month total/avg.** | | | | | | | | | | | **6,688** | **7,038** | **-5.0** | | |

Results in non-US currencies were converted to US dollars by applying a three-month average exchange rate for the corresponding quarter, except for the two Hong Kong-based companies, whose results were converted by using six-month average exchange rates. Average exchange rates were based on monthly 2012 and 2013 data from the US Federal Reserve. Company net profits shown here are attributable to shareholders. Net profit totals are approximate because not all companies follow the same accounting standard. [1] Sales of WKK's Manufacturing Div. [2] Profit of WKK's Manufacturing Div. included finance income and costs but excluded joint-venture items and income tax.

Net income rose about 6% compared with a sales decline of 8.5%. Significant profit growth at Shenzhen Kaifa and Fabrinet drove the increase.

For the first six months, net income of the nine providers totaled approximately $170 million for a net margin of about 2.7%. First-half net income climbed about 64% year over year thanks to a positive swing in net income at Fabrinet.

### Some highlights

• At **Cal-Comp Electronics**, Q2 sales of 30.34 billion baht (US$1.02 billion) were down 20.4% year over year (-16.8% in US dollars), and first-half sales of 59.94 billion baht (US$2.01 billion) fell 17.0% year over year (-13.4% in US dollars). The company said sales were lower mainly due to a continuation of weakened demand in the PC industry. In addition, the Thailand floods may also have affected the performance of certain products in the previous year because of shipments that were delayed from 2011.

For Q2, the company's gross margin came in at 4.93%, up 112 basis points year over year, and first-half gross margin stood at 4.33%, up 91 basis points year over year. The increase in gross margin mainly stemmed from a difference in product mix.

The company produced Q2 net income of 226 million baht (US$7.6 million), down 44% year over year (-41% in US dollars), and first-half net income of 500 million baht (US$16.8 million), down 21.5% (18.0% in US dollars). Q2 and first-half net profit declined from a year earlier mainly as a result of weakened economic conditions and demand worldwide.

• **Fabrinet** reported revenue of $159.9 million for its fiscal Q4 ended June 28. Sales rose 2.8% sequentially and 12.0% year over year. GAAP gross margin for the quarter was 10.7%, up 30 basis points sequentially but unchanged from the year-earlier period. GAAP net income amounted to $15.1 million, compared with $21.1 million in the prior quarter and $7.5 million in the same period a year ago. Non-GAAP net income was $12.4 million, or $0.35 a share, versus $11.5 million, or $0.33 a share, in the previous quarter, and $10.7 million, or $0.31 a share, a year earlier.

• **Integrated Micro-Electronics Inc.** recorded first-half sales of $350.5 million, up 7.6% year on year mainly due to the company's strong business expansion in Europe, Mexico and the Philippines. First-half net income of $2.1 million was 33% lower than the result posted for the same period last year primarily because of lower capacity utilization in IMI's China facilities.

IMI continues to expand its operations in Bulgaria and Mexico to accommodate additional orders from its customers in the automotive sector. But in China, the company has started to consolidate operations to lessen the impact on its bottom line. First-half revenue from IMI's China and Singapore operations declined 9% year over year primarily as a result of reduced sales in the telecom infrastructure segment. By contrast, first-half sales from operations in Europe and Mexico grew 37% from the year-earlier period due to continued expansion of the company's automotive business. Revenue from Philippine operations rose 11% year over year because of strong programs in the computing, consumer and industrial segments.

• **Pan-International Industrial**, a vertically integrated affiliate of EMS giant **Hon Hai Precision Industry**, turned in Q2 sales of NT$3.54 billion (US$118 million), 18.6% (17.2% in US dollars) higher than in the prior quarter but 8.2% (8.9% in US dollars) lower than a year earlier. Q2 gross profit amounted to NT$289.7 million, down 32% year over year, while operating profit equaled NT$19.5 million, down from NT$131.6 million in the same period a year ago.

First-half revenue of NT$6.52 billion (US$220 million) dropped 17.6% year over year (-17.7% in US dollars), while net income of NT$98.4 million (US$3.3 million) sank by 19.5%.

• At **PCI**, sales for its fiscal Q4 ended June 30 totaled $45.3 million, as revenue increased 11.6% sequentially but fell 35.1% year over year. The drop in revenue resulted from continuing weakness in orders from the company's EMS customers. Profit attributable to shareholders decreased to $270,000 from $2.6 million in the year-ago quarter. Gross margin for the quarter was 7.4%, down from 9.5% in the year-earlier period.

Of the $45.3 million in total revenue, $44.1 million came from EMS. PCI's EMS revenue declined 35.7% year over year, while EMS profit from operations dropped 98.6% to $35,000. Weaker demand from PCI's major EMS customers resulted in excess capacities and overhead, giving rise to a lower gross profit contribution versus the year-earlier quarter.

• **Shenzhen Kaifa Technology** reported Q2 sales of 3.73 billion RMB (US$606 million), up 0.7% sequentially (1.9% in US dollars) but down 15.0% year over year (-12.5% in US dollars). Yet Q2 net income of 55.0 million RMB (US$8.9 million) grew 69% from the prior quarter (71% in US dollars) and 168% from the year-earlier period (176% in US dollars). Net margin for the second quarter stood at 1.5%.

For the first six months of 2013, sales came to 7.43 billion RMB (US$1.20 billion), down 11.8% year over year (-9.9% in US dollars). The company earned first-half net income of 87.5 million RMB (US$14.2 million), up from 66.2 million RMB (US$10.5 million) in the year-ago period.

• **SVI** rang up Q2 sales of 1.88 billion baht (US$63 million), 16.4% above the prior quarter's level (16.1% in US dollars) but 9.5% lower than a year earlier (-5.3% in US dollars). During the quarter, the company launched new products and new customers to compensate for lower revenue from some existing customers due to the economic crisis in the European market. Q2 revenue was mainly driven by IP video, professional audio and medical business. The company recorded Q2 net profit of 189 million baht (US$6.3 million) for a net margin of 10.1%. Net profit increased 22.5% year on year (28.1% in US dollars) primarily because of an additional insurance payment and the reversal of a doubtful account charge. On a sequential basis, profit declined 15.5% (15.8% in US dollars) as a result of the reversal of a large doubtful account charge in Q1 and FX losses in Q2.

• **Universal Scientific Industrial**, the EMS unit of publicly held **Advanced Semiconductor Engineering**, generated Q2 revenue of NT$14.19 billion (US$475 million), down 13.4% sequentially (-14.4% in US dollars) but up 5.9% year over year (5.0% in US dollars). Q2 gross margin came in at 11.4%, down 10 basis points from the previous quarter and 140 basis points from a year earlier. Operating margin was 3.6% versus 4.8% in Q1 and 4.7% in the year-ago period. Net income in Q2 amounted to NT$457 million (US$15.3 million).

Sales from communications products accounted for 24% of USI's sales, 9 percentage points below the comparable share in Q1. For the computing, consumer, industrial, car and others segments, the percentage of total sales increased sequentially.

First-half sales of NT$30.57 billion (US$1.03 billion) rose 12.3% year over year (12.2% in US dollars), while first-half net income of NT$1.07 billion (US$36.1 million) grew 15.9% (16.0% in US dollars).

• **Venture** posted Q2 sales of S$587.7 million (US$471 million), up 10.8% sequentially (9.8% in US dollars) but down 3.9% year over year (-2.8% in US dollars). Q2 profit attributable to shareholders was S$30.1 million (US$24.1 million), up 7.3% sequentially (6.4% in US dollars) but down 10.6% from a year earlier (-9.5% in US dollars). The latter decline was primarily due to a higher income tax provision for Q2. Net margin for the quarter equaled 5.1%, down 20 basis points from Q1 and 40 basis points from the year-earlier period.

For the first six months, revenue totaled S$1.12 billion (US$899 million), down 5.7% from a year earlier (-4.2% in US dollars). The company recorded attributable profit of S$58.1 million (US$46.7 million), down 16.0% year on year (-14.6% in US dollars).

As a hybrid contract manufacturer, Venture engages in both EMS and ODM activities (see article on page 1). Since EMS business still represented about 65% of the company's 2012 sales, Venture was included in this analysis of Asia-based EMS providers.

• At **WKK International (Holdings)**, its OEM Manufacturing Division brought in first-half sales of HK$1.87 billion (US$241 million), representing a gain of 19.9% from the year-ago period (20.0% in US dollars) mainly because of an increase in the volume of orders from a major customer. The division's first-half operating profit of HK$26.0 million (US$3.3 million), including finance income and costs, improved by 54% as a result.

Despite the current economic conditions, the division is expected to secure more orders for the second half of 2013 compared with the first half, based on orders on hand.

• For the first six months, **Wong's International Holdings** reported sales of HK$1.70 billion (US$219 million), up 4.2% year over year. Operating margin came in at 2.4%, 40 basis points higher than in the same period a year ago. The company earned a first-half net profit of HK$28.6 million (US$3.7 million) attributable to shareholders compared with HK$28.4 million a year earlier.

Wong's operates two divisions: EMS and ODM. With first-half revenue of HK$1.69 billion, the EMS Division accounted for 99.6% of the company's sales for the period. EMS Division sales grew 5.0% year on year, while the division's reportable profit of HK$40.7 million (US$5.2 million) declined 1.6%. The decrease in profit was primarily attributed to an increase in labor costs and operation expenses. While the overall market environment was soft during the first six months, the division saw modest improvement in customer demand across different end-market segments.

In the first half, the ODM Division sustained a reportable loss of HK$10.5 million (US$1.3 million) on sales of HK$6.8 million (US$880,000).

## Latin America

# Costa Rica Draws Zollner

Mexico's star is rising as a regional source of EMS for supplying the US market. Given the number of EMS providers that have already set up in Mexico, it would appear that the country has a lock on serving as the low-cost alternative to China. But Mexico is not the only place where one can find lower labor rates and other economies in Latin America. Indeed, Germany's **Zollner Elektronik Group** passed up Mexico for Costa Rica.

Zollner, a top-15 EMS provider, recently announced that it selected Costa Rica for its first Latin American site, which will provide manufacturing and technical support services. The company plans to invest about $10 million in facilities and equipment and expects to employ 100 to 200 people there within three years. Within Costa Rica, Zollner has picked the city of Cartago for a new 5,000-$m^2$ building, Zollner's first step in the country. The greenfield plant is scheduled to come online in mid to late 2014, and the site will give engineering, R&D and procurement support to Zollner's Milpitas, CA, operations before then.

Once Zollner had made the move to open an NPI/low-volume facility in Milpitas, the company knew it needed a site in the US or a lower-cost location to supply Milpitas customers with volume production. In the end, Zollner considered three options: Southeastern US near the automotive industry, Mexico or Costa Rica. The company said it chose Costa Rica for the country's stability, educational system, manufacturing resources and strategic location.

Costa Rica is Latin America's oldest democracy, and a World Bank study ranked it second in Latin America for political stability. As for education, public education is free and mandatory, and Costa Rica's educational system was ranked 21st in the world, the highest in Latin America and above US schools, which came in 28th, according to a report by the World Economic Forum.

Zollner also found that the country offers the necessary human resources. "We are not one of the big top-five EMS providers who needs thousands of people. For a big EMS guy, Costa Rica is for sure too small," said Markus Aschenbrenner, director of business development at Zollner and president and CEO of its US operations. "But with the size of our company and the products we are looking for, I think there are enough resources available."

Costa Rica's strategic location in the middle of the Americas appealed to Zollner as well. Traveling by Caribbean or Pacific Ocean routes, cargo ships from Costa Rica can reach Miami or Los Angeles in eight to 12 days, Aschenbrenner noted. Costa Rica's midway location also puts Zollner in a position to pursue the South American market in the future.

Zollner's decision hinged on other factors too, and labor costs were an obvious one. Costa Rica's labor rates are comparable to those in Mexico, according to Aschenbrenner, though pay scales can vary in Mexico depending on where you look. Government support was also important to Zollner, and Costa Rica offers a number of incentives for foreign investment.

But no place is perfect, and Costa Rica is not without disadvantages. For an EMS provider, inbound logistics are not set up as they would be in, say, the US or Mexico. Costa Rica lacks a distribution network to supply components locally. Another issue involves the supply of metal parts, plastics and other items for Zollner's system integration work. "There is definitely the need to select the right suppliers and develop them a little bit" to meet Zollner's needs, said Aschenbrenner. "So there's a lot of groundwork that we need to do." Costa Rica has become a center for medical device manufacturing, and Zollner intends to leverage local plastics and metal suppliers that already serve the medical industry there.

During a rather cursory search, *MMI* found two EMS providers in Costa Rica, although there are companies doing other forms of contract manufacturing including medical work. Given Costa Rica's advantages, why haven't other EMS companies set up shop in Costa Rica? Aschenbrenner believes that the largest providers have not come to Costa Rica because of its size and distance to the US.

Still, it appears that Zollner is not the only EMS provider that has put Costa Rica on its radar screen. The **Costa Rican Investment Promotion Agency** (CINDE) told Aschenbrenner that there is interest in Costa Rica from other EMS providers.

### Another investment in Costa Rica

Earlier this year, **General Microcircuits, Inc.** (Mooresville, NC), one of the EMS providers currently operating in Costa Rica, moved into a new facility in Coyol, Alajuela. This company-owned facility of 2,000 $m^2$ doubled GMI's manufacturing space in Costa Rica and added three floors of office space. At the facility's inauguration in January, GMI put its investment in the new facility at about $3 million and said it expected to hire 150 more people there by the end of next year.

## News

# *Jabil Factory Accused of Labor Violations*

**China Labor Watch** (New York NY), a labor watchdog group, has charged **Jabil's** factory in Wuxi, China, with a series of labor violations. Based on an undercover investigation, a new CLW report lists a number of violations that have allegedly occurred at the Jabil Green Point factory including unpaid overtime; over 100 hours of monthly overtime, usually mandatory; more than 11 hours of standing work per day; inadequate training; and hiring discrimination.

The factory, part of Jabil's Materials Technology Group, is an **Apple** supplier, and Jabil and Apple have each sent an audit team to look into CLW's claims.

In a statement, Jabil said it "is committed to ensuring every employee is provided a safe working environment where they are treated fairly, with dignity and respect. We take seriously any allegation that we are not fulfilling that commitment and are taking immediate action to ensure recent allegations are thoroughly investigated and, if found to be credible, corrected."

Jabil pointed out that its VP of Social Responsibility, Eric Austermann, conducted an audit of the Wuxi factory in August. The audit found some issues cited in the report, such as unpaid meeting times, and corrective action began immediately.

In July, CLW released the results of its investigation of three **Pegatron** factories, which also supply Apple.

*OEM divestiture*…**Ascom Wireless Solutions** (Dübendorf, Switzerland), a provider of wireless solutions and network testing, has outsourced production and repair in its Herrljunga, Sweden, factory to **Fideltronik Group** (Sucha Beskidzka, Poland). An agreement between the two companies calls for a Fideltronik affiliate to take over the factory as of Sept. 1. As part of the transaction, 150 Ascom employees are to join Fideltronik.

*Another transaction*…Vinu Patel, CEO and owner of **Anuva Manufacturing Services** (West Melbourne, FL) recently purchased controlling interest in **TriE Medical** (Morrisville, NC), a medical device development firm. Earlier in the year, the two companies formed a partnership to offer a complete turnkey solution from design to manufacturing.

*Allliance*…**Absolute EMS** (Santa Clara, CA) has partnered with **Ionics EMS** (Calamba, Laguna, Philippines) to increase Absolute's production capabilities and capacity for Absolute customers that must scale volumes quickly and easily.

*New facilities*…**Plexus** (Neenah, WI) has agreed to lease a 265,000-ft$^2$ manufacturing facility in Guadalajara, Mexico. Construction of the leased building is expected to be completed during the second quarter of calendar 2014.…**Shenzhen Kaifa Technology** (Shenzhen, China) recently celebrated the completion of the first phase of its new operation in Huizhou, a city within China's Guangdong province. The company expects mobile phone production there to reach three million per month after September. Its Huizhou complex will occupy 125,000 m$^2$ with a total floor area of 180,000 m$^2$. Shenzhen Kaifa plans to invest a total of 1.6 billion RMB ($260 million) in the project, which will create about 6,000 jobs. When in full production, the operation will have an output of 6 to 10 billion RMB ($976 million to $1.6 billion).…Contract manufacturer **Darekon** (Espoo, Finland) has expanded its operations in Poland with a second factory, a 2,400-m$^2$ facility in Gdansk.

*Slated for closure*...Jabil intends to close its Tempe, AZ, plant within the next 12 months, *The Arizona Republic* reported.

*Correction*…In the August edition on page 4, the name **Benchmark** was used by mistake in a third-column paragraph describing guidance issued by **Celestica**. The first sentence of that paragraph should have read: On a sequential basis, Celestica expects relatively flat Q3 revenue from communications, mid single-digit growth in the diversified and storage end markets for Q3, and double-digit declines in the server and consumer segments.

**Editor and Publisher:** John Tuck
**Circulation Director:** Ann Connors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**E-mail:** jbt@mfgmkt.com
**Web site:** www.mfgmkt.com