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

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**FORM 10-Q**

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(Mark One)

**Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the quarterly period ended March 27, 2020

OR

**Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 001-34775

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**FABRINET**

(Exact name of registrant as specified in its charter)

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Cayman Islands  
(State or other jurisdiction of  
incorporation or organization)

98-1228572  
(I.R.S. Employer  
Identification No.)

c/o Intertrust Corporate Services (Cayman) Limited  
190 Elgin Avenue  
George Town  
Grand Cayman  
Cayman Islands  
(Address of principal executive offices)

KY1-9005  
(Zip Code)

+66 2-524-9600  
(Registrant's telephone number, including area code)

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

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Securities registered pursuant to Section 12(b) of the Act:

<u>Title of each class</u>	<u>Trading Symbol(s)</u>	<u>Name of each exchange on which registered</u>
Ordinary Shares, \$0.01 par value	FN	New York Stock Exchange

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 (the "Exchange Act") during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days: Yes  No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer	<input checked="" type="checkbox"/>	Accelerated filer	<input type="checkbox"/>
Non-accelerated filer	<input type="checkbox"/>	Smaller reporting company	<input type="checkbox"/>
		Emerging growth company	<input type="checkbox"/>

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

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

As of April 24, 2020, the registrant had 36,722,004 ordinary shares, \$0.01 par value, outstanding.

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**FABRINET  
FORM 10-Q  
QUARTER ENDED MARCH 27, 2020**

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**PART I: FINANCIAL INFORMATION**

**ITEM 1. FINANCIAL STATEMENTS**

**FABRINET**

**CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited)**

<i>(in thousands of U.S. dollars, except share data and par value)</i>	<b>March 27, 2020</b>	<b>June 28, 2019</b>
<b>Assets</b>		
<b>Current assets</b>		
Cash and cash equivalents	\$ 224,138	\$ 180,839
Short-term restricted cash	7,402	—
Short-term investments	233,622	256,493
Trade accounts receivable, net	283,467	260,602
Contract assets	16,413	12,447
Inventories	290,208	293,612
Other receivable	24,310	—
Prepaid expenses	4,524	8,827
Other current assets	8,774	11,015
<b>Total current assets</b>	<u>1,092,858</u>	<u>1,023,835</u>
<b>Non-current assets</b>		
Long-term restricted cash	—	7,402
Property, plant and equipment, net	218,043	210,686
Intangibles, net	3,999	3,887
Operating right-of-use assets	7,175	—
Goodwill	3,571	3,705
Deferred tax assets	4,353	5,679
Other non-current assets	262	124
<b>Total non-current assets</b>	<u>237,403</u>	<u>231,483</u>
<b>Total Assets</b>	<u>\$1,330,261</u>	<u>\$1,255,318</u>
<b>Liabilities and Shareholders' Equity</b>		
<b>Current liabilities</b>		
Long-term borrowings, current portion, net	\$ 12,156	\$ 3,250
Trade accounts payable	240,028	257,617
Contract liabilities	1,941	2,239
Operating lease liabilities, current portion	1,893	—
Income tax payable	2,857	1,801
Accrued payroll, bonus and related expenses	19,959	16,510
Accrued expenses	19,798	8,997
Other payables	28,819	22,634
<b>Total current liabilities</b>	<u>327,451</u>	<u>313,048</u>
<b>Non-current liabilities</b>		
Long-term borrowings, non-current portion, net	42,553	57,688
Deferred tax liability	3,684	3,561
Operating lease liabilities, non-current portion	5,024	—
Severance liabilities	16,143	15,209
Other non-current liabilities	1,997	2,713
<b>Total non-current liabilities</b>	<u>69,401</u>	<u>79,171</u>
<b>Total Liabilities</b>	<u>396,852</u>	<u>392,219</u>
Commitments and contingencies (Note 19)		
<b>Shareholders' equity</b>		
Preferred shares (5,000,000 shares authorized, \$0.01 par value; no shares issued and outstanding as of March 27, 2020 and June 28, 2019)	—	—
Ordinary shares (500,000,000 shares authorized, \$0.01 par value; 38,460,931 shares and 38,230,753 shares issued as of March 27, 2020 and June 28, 2019, respectively; and 36,716,828 shares and 36,841,650 shares outstanding as of March 27, 2020 and June 28, 2019, respectively)	385	382
Additional paid-in capital	171,870	158,299
Less: Treasury shares, at cost (1,744,103 shares and 1,389,103 shares as of March 27, 2020 and June 28, 2019, respectively)	(68,501)	(47,779)
Accumulated other comprehensive loss	(10,383)	(2,386)
Retained earnings	840,038	754,583
<b>Total Shareholders' Equity</b>	<u>933,409</u>	<u>863,099</u>
<b>Total Liabilities and Shareholders' Equity</b>	<u>\$1,330,261</u>	<u>\$1,255,318</u>

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

**FABRINET**
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (unaudited)**

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>March 27, 2020</b>	<b>March 29, 2019</b>	<b>March 27, 2020</b>	<b>March 29, 2019</b>
<i>(in thousands of U.S. dollars, except per share data)</i>				
Revenues	\$ 411,210	\$ 398,951	\$ 1,236,723	\$ 1,179,208
Cost of revenues	(366,874)	(352,193)	(1,097,242)	(1,046,610)
Gross profit	44,336	46,758	139,481	132,598
Selling, general and administrative expenses	(17,111)	(14,132)	(50,189)	(41,296)
Expenses related to reduction in workforce	—	(323)	(16)	(727)
Operating income	27,225	32,303	89,276	90,575
Interest income	2,042	2,144	6,080	4,770
Interest expense	(238)	(1,423)	(2,812)	(3,673)
Foreign exchange loss, net	(8)	(3,055)	(2,949)	(408)
Other income, net	203	159	977	798
Income before income taxes	29,224	30,128	90,572	92,062
Income tax expense	(957)	(1,493)	(5,117)	(4,064)
Net income	28,267	28,635	85,455	87,998
Other comprehensive income (loss), net of tax:				
Change in net unrealized (loss) gain on available-for-sale securities	(1,356)	513	(1,403)	1,399
Change in net unrealized loss on derivative instruments	(6,569)	(1)	(6,719)	(2)
Change in net retirement benefits plan – prior service cost	294	—	478	—
Change in foreign currency translation adjustment	(600)	486	(353)	(219)
Total other comprehensive (loss) income, net of tax	(8,231)	998	(7,997)	1,178
Net comprehensive income	\$ 20,036	\$ 29,633	\$ 77,458	\$ 89,176
<b>Earnings per share</b>				
Basic	\$ 0.76	\$ 0.78	\$ 2.31	\$ 2.39
Diluted	\$ 0.75	\$ 0.76	\$ 2.27	\$ 2.35
<b>Weighted-average number of ordinary shares outstanding (thousands of shares)</b>				
Basic	36,987	36,891	36,970	36,786
Diluted	37,797	37,539	37,696	37,383

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

**FABRINET**
**CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (unaudited)**
**For the Three Months Ended March 27, 2020**

	Ordinary Shares		Additional Paid-in Capital	Treasury Shares	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total
	Shares	Amount					
<i>(in thousands of U.S. dollars, except share data)</i>							
Balances at December 27, 2019	38,408,890	\$ 384	\$ 166,103	\$(47,779)	\$ (2,152)	\$ 811,771	\$ 928,327
Net income	—	—	—	—	—	28,267	28,267
Other comprehensive loss	—	—	—	—	(8,231)	—	(8,231)
Share-based compensation	—	—	6,118	—	—	—	6,118
Issuance of ordinary shares	52,041	1	(1)	—	—	—	—
Repurchase of 355,000 shares held as treasury shares	—	—	—	(20,722)	—	—	(20,722)
Tax withholdings related to net share settlement of restricted share units	—	—	(350)	—	—	—	(350)
Balances at March 27, 2020	<u>38,460,931</u>	<u>\$ 385</u>	<u>\$ 171,870</u>	<u>\$(68,501)</u>	<u>\$ (10,383)</u>	<u>\$ 840,038</u>	<u>\$ 933,409</u>

**For the Nine Months Ended March 27, 2020**

	Ordinary Shares		Additional Paid-in Capital	Treasury Shares	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total
	Shares	Amount					
<i>(in thousands of U.S. dollars, except share data)</i>							
Balances at June 28, 2019	38,230,753	\$ 382	\$ 158,299	\$(47,779)	\$ (2,386)	\$ 754,583	\$ 863,099
Net income	—	—	—	—	—	85,455	85,455
Other comprehensive loss	—	—	—	—	(7,997)	—	(7,997)
Share-based compensation	—	—	18,301	—	—	—	18,301
Issuance of ordinary shares	230,178	3	(3)	—	—	—	—
Repurchase of 355,000 shares held as treasury shares	—	—	—	(20,722)	—	—	(20,722)
Tax withholdings related to net share settlement of restricted share units	—	—	(4,727)	—	—	—	(4,727)
Balances at March 27, 2020	<u>38,460,931</u>	<u>\$ 385</u>	<u>\$ 171,870</u>	<u>\$(68,501)</u>	<u>\$ (10,383)</u>	<u>\$ 840,038</u>	<u>\$ 933,409</u>

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

**FABRINET**
**CONDENSED CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY (unaudited) (Continued)**
**For the Three Months Ended March 29, 2019**

	Ordinary Shares		Additional Paid-in Capital	Treasury Shares	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total
	Shares	Amount					
<i>(in thousands of U.S. dollars, except share data)</i>							
Balances at December 28, 2018	38,138,159	\$ 381	\$151,639	\$(42,401)	\$ (1,077)	\$692,991	\$801,533
Net income	—	—	—	—	—	28,635	28,635
Other comprehensive income	—	—	—	—	998	—	998
Share-based compensation	—	—	4,424	—	—	—	4,424
Issuance of ordinary shares	78,072	1	(1)	—	—	—	—
Repurchase of 100,000 shares held as treasury shares	—	—	—	(5,378)	—	—	(5,378)
Tax withholdings related to net share settlement of restricted share units	—	—	(1,324)	—	—	—	(1,324)
Balances at March 29, 2019	<u>38,216,231</u>	<u>\$ 382</u>	<u>\$154,738</u>	<u>\$(47,779)</u>	<u>\$ (79)</u>	<u>\$721,626</u>	<u>\$828,888</u>

**For the Nine Months Ended March 29, 2019**

	Ordinary Shares		Additional Paid-in Capital	Treasury Shares	Accumulated Other Comprehensive Income (Loss)	Retained Earnings	Total
	Shares	Amount					
<i>(in thousands of U.S. dollars, except share data)</i>							
Balances at June 29, 2018	37,723,733	\$ 377	\$151,797	\$(42,401)	\$ (1,257)	\$632,423	\$740,939
Net income	—	—	—	—	—	87,998	87,998
Other comprehensive income	—	—	—	—	1,178	—	1,178
Cumulative effect adjustment from adoption of ASC 606	—	—	—	—	—	1,205	1,205
Share-based compensation	—	—	13,373	—	—	—	13,373
Issuance of ordinary shares	492,498	5	(5)	—	—	—	—
Repurchase of 100,000 shares held as treasury shares	—	—	—	(5,378)	—	—	(5,378)
Tax withholdings related to net share settlement of restricted share units	—	—	(10,427)	—	—	—	(10,427)
Balances at March 29, 2019	<u>38,216,231</u>	<u>\$ 382</u>	<u>\$154,738</u>	<u>\$(47,779)</u>	<u>\$ (79)</u>	<u>\$721,626</u>	<u>\$828,888</u>

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

**FABRINET**
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited)**

	<b>Nine Months Ended</b>	
	<b>March 27, 2020</b>	<b>March 29, 2019</b>
<i>(in thousands of U.S. dollars)</i>		
<b>Cash flows from operating activities</b>		
Net income for the period	\$ 85,455	\$ 87,998
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	23,115	22,521
Loss on disposal of property, plant and equipment	444	81
Loss on disposal of intangibles	—	149
Gain from sales and maturities of available-for-sale securities	(93)	(196)
Accretion of premiums on short-term investments	(624)	(604)
Amortization of deferred debt issuance costs	18	—
(Reversal) allowance for doubtful accounts	(17)	12
Unrealized loss (gain) on exchange rate and fair value of foreign currency forward contracts	942	(5,351)
Unrealized loss on fair value of interest rate swaps	1,672	1,564
Amortization of fair value at hedge inception of interest rate swaps	(838)	—
Share-based compensation	18,301	13,373
Deferred income tax	1,335	438
Other non-cash expenses	(559)	(699)
Changes in operating assets and liabilities		
Trade accounts receivable	(23,136)	(17,942)
Contract assets	(3,966)	(666)
Inventories	3,404	(36,418)
Other current assets and non-current assets	5,830	(1,568)
Trade accounts payable	(15,571)	37,576
Contract liabilities	(298)	—
Income tax payable	1,056	1,942
Severance liabilities	2,266	1,841
Other current liabilities and non-current liabilities	5,712	1,453
Net cash provided by operating activities	<u>104,448</u>	<u>105,504</u>
<b>Cash flows from investing activities</b>		
Purchase of short-term investments	(123,980)	(202,328)
Proceeds from sales of short-term investments	48,808	85,941
Proceeds from maturities of short-term investments	97,358	50,370
Funds provided to customer to support transfer of manufacturing operations (Note 9)	(24,310)	—
Purchase of property, plant and equipment	(27,482)	(13,211)
Purchase of intangibles	(797)	(290)
Proceeds from disposal of property, plant and equipment	1,482	473
Net cash used in investing activities	<u>(28,921)</u>	<u>(79,045)</u>
<b>Cash flows from financing activities</b>		
Payment of debt issuance costs	(153)	—
Proceeds from long-term borrowings	60,938	—
Repayment of long-term borrowings	(67,032)	(2,438)
Repayment of finance lease liabilities	(304)	(342)
Repurchase of ordinary shares	(20,722)	(5,378)
Release of restricted cash held in connection with business acquisition	—	(3,478)
Withholding tax related to net share settlement of restricted share units	(4,727)	(10,427)
Net cash used in financing activities	<u>(32,000)</u>	<u>(22,063)</u>
<b>Net increase in cash, cash equivalents and restricted cash</b>	<u>43,527</u>	<u>4,396</u>
<b>Movement in cash, cash equivalents and restricted cash</b>		
Cash, cash equivalents and restricted cash at beginning of period	188,241	161,433
Increase in cash, cash equivalents and restricted cash	43,527	4,396
Effect of exchange rate on cash, cash equivalents and restricted cash	(228)	578
<b>Cash, cash equivalents and restricted cash at end of period</b>	<u>\$ 231,540</u>	<u>\$ 166,407</u>
<b>Non-cash investing and financing activities</b>		
Construction, software and equipment-related payables	\$ 11,906	\$ 3,286

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.



**FABRINET****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (unaudited) (Continued)**

The following table provides a reconciliation of cash, cash equivalents and restricted cash reported within the unaudited condensed consolidated balance sheets that sum to the total of the same amounts shown in the unaudited condensed consolidated statements of cash flows:

<i>(amount in thousands)</i>	<u>As of March 27, 2020</u>	<u>As of March 29, 2019</u>
Cash and cash equivalents	\$224,138	\$166,407
Restricted cash	7,402	—
Cash, cash equivalents and restricted cash	<u>\$231,540</u>	<u>\$166,407</u>

The accompanying notes are an integral part of these unaudited condensed consolidated financial statements.

**FABRINET**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (unaudited)**  
**(in thousands of U.S. dollars unless otherwise noted)**

**1. Business and organization**

**General**

Fabrinet (“Fabrinet” or the “Parent Company”) was incorporated on August 12, 1999, and commenced operations on January 1, 2000. The Parent Company is an exempted company incorporated in the Cayman Islands, British West Indies. The “Company” refers to Fabrinet and its subsidiaries as a group.

The Company provides advanced optical packaging and precision optical, electro-mechanical and electronic manufacturing services to original equipment manufacturers (“OEMs”) of complex products, such as optical communication components, modules and sub-systems, industrial lasers, automotive components, medical devices and sensors. The Company offers a broad range of advanced optical and electro-mechanical capabilities across the entire manufacturing process, including process design and engineering, supply chain management, manufacturing, complex printed circuit board assembly, advanced packaging, integration, final assembly and testing. The Company focuses primarily on the production of low-volume, high-mix products. The principal subsidiaries of Fabrinet include Fabrinet Co., Ltd. (“Fabrinet Thailand”), Casix, Inc. (“Casix”), Fabrinet West, Inc. (“Fabrinet West”) and Fabrinet UK Limited (“Fabrinet UK”).

**2. Accounting policies**

***Basis of presentation***

The accompanying unaudited condensed consolidated financial statements for Fabrinet as of March 27, 2020 and for the three and nine months ended March 27, 2020 and March 29, 2019 include normal recurring adjustments necessary for a fair statement of the financial statements set forth herein, in accordance with accounting principles generally accepted in the United States of America (“U.S. GAAP”) for interim financial information and the rules and regulations of the Securities and Exchange Commission (“SEC”). Accordingly, such information does not include all of the information and footnotes required by U.S. GAAP for annual financial statements. For further information, please refer to the consolidated financial statements and footnotes thereto included in Fabrinet’s Annual Report on Form 10-K for the year ended June 28, 2019.

The balance sheet as of June 28, 2019 has been derived from the audited financial statements at that date but does not include all of the information and footnotes required by U.S. GAAP for complete financial statements.

The results for the three and nine months ended March 27, 2020 may not be indicative of results for the year ending June 26, 2020 or any future periods.

***Use of estimates***

The preparation of the Company’s unaudited condensed consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the date of the financial statements, and the reported amount of total revenues and expenses during the year. The Company bases estimates on historical experience and various assumptions about the future that are believed to be reasonable based on available information. The Company’s reported financial position or results of operations may be materially different under different conditions or when using different estimates and assumptions, particularly with respect to significant accounting policies, which are discussed below. Significant assumptions are used in accounting for share-based compensation, allowance for doubtful accounts, income taxes, inventory obsolescence, goodwill and valuation of intangible assets related to business acquisitions, among others. Due to the inherent uncertainty involved in making estimates, actual results reported in future periods may be different from these estimates. In the event that estimates or assumptions prove to be different from actual results, adjustments will be made in subsequent periods to reflect more current information.

**Fiscal years**

The Company utilizes a 52 to 53-week fiscal year ending on the Friday in June closest to June 30. The three months ended March 27, 2020 and March 29, 2019 each consisted of 13 weeks. The nine months ended March 27, 2020 and March 29, 2019 each consisted of 39 weeks. Fiscal year 2020 will be comprised of 52 weeks and will end on June 26, 2020.

**Reclassifications**

For presentation purposes, certain prior period amounts have been reclassified to conform to the current period presentation. These reclassifications do not affect the Company's net income, cash flows or stockholders' equity.

**Changes in accounting policies**

Except for the adoption of the new lease accounting standard and the derivatives and hedging standard described below, the Company has consistently applied its accounting policies to all periods presented in these unaudited condensed consolidated financial statements.

**Concentration of credit risk**

Financial instruments that potentially subject the Company to concentrations of credit risk consist of cash and cash equivalents, short-term investments, derivatives, accounts receivable and contract assets.

Cash, cash equivalents and short-term investments are maintained with several financial institutions. Deposits held with banks may exceed the amount of insurance provided on such deposits. Generally, these deposits may be redeemed upon demand and are maintained with financial institutions with reputable credit and therefore bear minimal credit risk. The Company seeks to mitigate its credit risks by spreading such risks across multiple counterparties and monitoring the risk profiles of these counterparties. The Company limits its short-term investments in marketable securities to securities with a maturity not in excess of three years and securities that are rated A1, P-1, F1, or better.

The Company enters into derivative contracts with financial institutions with reputable credit and monitors the credit profiles of these counterparties.

The Company performs ongoing credit evaluations for credit worthiness of its customers and usually does not require collateral from its customers. Management has implemented a program to closely monitor near term cash collection and credit exposures to mitigate any material losses.

**Adoption of new accounting standards**

On June 29, 2019, the Company adopted the new lease accounting standard, Accounting Standards Codification ("ASC") Topic 842, which provides guidance for the recognition and disclosure of lease arrangements. The Company adopted ASC 842 using the modified retrospective transition approach. Accordingly, the Company's comparative financial statements as of June 28, 2019 have not been adjusted. ASC 842 also provides practical expedients for the Company's ongoing accounting. The Company elected the short-term lease recognition exemption for its operating leases with a term of less than 12 months, which will not require recognition of right of use ("ROU") assets or lease liabilities for these leases.

For periods prior to adoption of ASC 842, the Company is required to present disclosures in accordance with ASC Topic 840. Future minimum lease payments due under non-cancelable operating leases as of June 28, 2019 were as follows:

<i>(amount in thousands)</i>	
2020	\$1,746
2021	1,342
2022	1,219
2023	1,172
Thereafter	230
Total future minimum operating lease payments	<u>\$5,709</u>

The most significant impact of the adoption of ASC 842 was the recognition of ROU assets and lease liabilities for operating leases with a term of greater than 12 months, while the accounting for finance leases will remain substantially unchanged. See Note 11 for further details.

On June 29, 2019, the Company also adopted Accounting Standards Update (“ASU”) 2017-12, “Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities.” ASU 2017-12 simplifies existing hedge accounting guidance in order to better portray the economic impact of risk management activities in the financial statements, including eliminating the separate measurement and presentation of hedge ineffectiveness. Prior to the adoption of ASU 2017-12, the Company was required to separately measure and reflect the amount by which the hedging instrument did not offset the changes in the fair value or cash flows of hedged items, and to record the ineffective portion as earnings. Upon the adoption of ASU 2017-12, the Company no longer recognizes hedge ineffectiveness as earnings, but instead records the entire changes in the fair value of the hedged instruments as other comprehensive income. Amounts recorded as other comprehensive income are subsequently reclassified to earnings in the same income statement line item that is used to present the earnings effect of the hedged item when the hedged item affects earnings. See Note 6 for further details.

In March 2020, the Financial Accounting Standards Board (“FASB”) issued ASU 2020-04, “Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting,” which temporarily simplifies the accounting for contract modifications, including hedging relationships, due to the transition from LIBOR and other interbank offered rates to alternative reference interest rates. For example, entities can elect not to remeasure the contracts at the modification date or reassess a previous accounting determination if certain conditions are met. Additionally, entities can elect to continue applying hedge accounting for hedging relationships affected by reference rate reform if certain conditions are met. The new standard was effective upon issuance and generally can be applied to applicable contract modifications through December 31, 2022. This ASU was effective for the Company in the third quarter of fiscal 2020 with no impact to the Company’s unaudited condensed consolidated financial statements.

#### ***New accounting pronouncements – not yet adopted by the Company***

In December 2019, the FASB issued ASU 2019-12, “Income Taxes (Topic 740): Simplifying the Accounting for Income Taxes.” The amendments in this update simplify the accounting for income taxes by removing certain exceptions to the general principles in Topic 740. The amendments also improve consistent application of and simplify U.S. GAAP for other areas of Topic 740 by clarifying and amending existing guidance. For public business entities, the amendments in this update are effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2020. This ASU will be effective for the Company in the first quarter of fiscal 2022. Early adoption is permitted. The Company is currently evaluating the impact of the adoption of this update on its condensed consolidated financial statements.

In August 2018, the FASB issued ASU 2018-13, “Fair Value Measurement (Topic 820), Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement.” ASU 2018-13 is intended to improve the effectiveness of disclosures in the notes to the financial statements, including (1) the development of a framework that promotes consistent decisions by the FASB about disclosure requirements and (2) the appropriate exercise of discretion by reporting entities. The amendment modifies the disclosure requirements on transferring between level 1 and level 2 and valuation processes of level 3 fair value measurements. This update is effective for all entities for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. This ASU will be effective for the Company in the first quarter of fiscal 2021. The Company is currently evaluating the impact of the adoption of this update on its condensed consolidated financial statements.

In January 2017, the FASB issued ASU 2017-04, “Intangibles—Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment.” ASU 2017-04 modifies the concept of impairment assessment from the condition that exists when the carrying amount of goodwill exceeds its implied fair value to the condition that exists when the carrying amount of a reporting unit exceeds its fair value. Public companies that are SEC filers should adopt the amendment for annual and any interim goodwill impairment tests in fiscal years beginning after December 15, 2019. Early adoption is permitted for interim or annual goodwill impairment tests performed on testing dates after January 1, 2017. This ASU will be effective for the Company in the first quarter of fiscal 2021. The Company does not expect this update will impact its condensed consolidated financial statements.

In June 2016, the FASB issued ASU 2016-13, “Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments,” which establishes a new credit impairment model for financial assets measured at amortized cost and available-for-sale debt securities. The FASB issued subsequent amendments to Topic 326, including ASU 2018-19, ASU 2019-04, ASU 2019-05, ASU 2019-11 and ASU 2020-02, which provided further

guidance and transition relief. For public business entities, this update is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. This ASU will be effective for the Company in the first quarter of fiscal 2021. Early adoption is permitted. The Company is currently evaluating the impact of the adoption of this update on its condensed consolidated financial statements.

### **3. Revenues from contracts with customers**

The Company derives revenues primarily from the assembly of products under supply agreements with its customers and the fabrication of customized optics and glass. The Company recognizes revenue relating to contracts with customers that depicts the transfer of promised goods or services to customers in an amount reflecting the consideration to which the Company expects to be entitled in exchange for such goods or services. In order to meet this requirement, the Company applies the following five steps: (1) identify the contract with a customer, (2) identify the performance obligations under the contract, (3) determine the transaction price, (4) allocate the transaction price to the performance obligations under the contract, and (5) recognize revenue when a performance obligation is satisfied. Revenue is recognized net of any taxes collected from customers, which is subsequently remitted to governmental authorities.

A performance obligation is a contractual promise to transfer a distinct good or service to the customer. In contracts with multiple performance obligations, the Company identifies each performance obligation and evaluates whether the performance obligation is distinct within the context of the contract at contract inception. The majority of the Company's contracts have a single performance obligation, as the promise to transfer the individual goods or services is not separately identifiable from other promises under the contracts and, therefore, is not distinct.

The Company manufactures products that are customized to customers' specifications. However, control of the products is typically transferred to the customer at the point in time the product is either shipped or delivered, depending on the terms of the arrangement, as the criteria for recognizing revenue over time are not met. Based on a review of its contracts, the Company determined that it does not have contractual rights to bill profit for work in progress in the event of a contract termination, an event which is expected to be infrequent. Further, in limited circumstances, substantive acceptance by the customer will result in the deferral of revenue until acceptance is formally received from the customer. Judgment may be required in determining if the acceptance clause provides for substantive acceptance.

Certain customers may request the Company to store finished products purchased by them at the Company's warehouse. In these instances, the Company receives a written request from the customer asking the Company to hold the inventory at the Company's warehouse, and the ordered goods cannot be used to fulfill other customer orders. In these situations, revenue is only recognized when the goods are completed and ready for shipment and transferred to the Company's warehouse.

Our customers generally are obligated to purchase finished goods that we have manufactured according to their demand requirements. Materials that are not consumed by our customers within a specified period of time, or that are no longer required due to a product's cancellation or end-of-life, are typically designated as excess or obsolete inventory under our contracts. After materials are designated as either excess or obsolete inventory, our customers are typically required to purchase such inventory from us even if they have chosen to cancel production of the related products. The excess or obsolete inventory is shipped to the customer and revenue is recognized upon shipment.

A contract's transaction price is allocated to each distinct performance obligation and recognized as revenue when, or as, the performance obligation is satisfied. In determining the transaction price, the Company evaluates whether the price is subject to refund or adjustment to determine the net consideration to which the Company expects to be entitled. The Company generally does not grant return privileges other than for defective products during the warranty period. The Company generally provides a warranty of between one to five years on the product.

The Company has applied the practical expedient to not adjust the amount of revenue to be recognized due to the effects of a significant financing component when the Company expects, at contract inception, that the period between the transfer of goods and/or services and the payment for those goods and/or services will be less than one year.

#### ***Warranty provision***

Provisions for estimated expenses relating to product warranties are made at the time the products are sold using historical experience. Generally, this warranty is limited to workmanship, and the Company's liability is capped at the price of the product. The provisions will be adjusted when experience indicates an expected settlement will differ from initial estimates.

**Contract assets and liabilities**

A contract asset is recognized when the Company has recognized revenues prior to generating an invoice for payment. Contract assets are classified separately within the unaudited condensed consolidated balance sheets and transferred to accounts receivable when rights to payment become unconditional. During the nine months ended March 27, 2020, the Company had no impairment for contract assets recognized.

A contract liability is recognized when the Company has advance payment arrangements with customers. The contract liabilities balance is normally recognized as revenue within six months.

The following tables summarize the activity in the Company's contract assets and contract liabilities during the nine months ended March 27, 2020:

<i>(amount in thousands)</i>	<b>Contract Assets</b>
Beginning balance, June 28, 2019	\$ 12,447
Revenue recognized	58,037
Amounts collected or invoiced	(54,071)
Ending balance, March 27, 2020	<u>\$ 16,413</u>

<i>(amount in thousands)</i>	<b>Contract Liabilities</b>
Beginning balance, June 28, 2019	\$ 2,239
Advance payment received during the period	6,857
Revenue recognized	(7,155)
Ending balance, March 27, 2020	<u>\$ 1,941</u>

**Contract costs**

The incremental costs of obtaining a contract with a customer are recognized as an asset (not expensed as incurred) if such costs are expected to be recovered. Incremental costs of obtaining a contract are costs that the Company would not have incurred if the contract had not been obtained (e.g., sales commissions or similar incentive payments linked directly to new or modified customer contracts). Costs that would have been incurred regardless of whether a customer contract was obtained (e.g., costs of pursuing the contact, legal advice, etc.) are expensed as incurred, unless such costs are explicitly chargeable to the customer. During the nine months ended March 27, 2020, the Company did not have any incremental costs of obtaining a contract.

**Shipping and handling**

Shipping costs billed to customers are recorded as revenue. Shipping and handling expense related to costs incurred to deliver product are recognized within cost of goods sold. The Company accounts for shipping and handling activities that occur after control has transferred as a fulfillment cost as opposed to a separate performance obligation, and the costs of shipping and handling are recognized concurrently with the related revenue.

**Revenue by geographic area**

Total revenues are attributed to a particular geographic area based on the bill-to-location of the Company's customers. The Company operates in three geographic regions: North America, Asia-Pacific and Europe.

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The following tables present total revenues by geographic region:

<i>(amount in thousands, except percentages)</i>	<b>Three Months Ended March 27, 2020</b>	<b>As a % of Total Revenues</b>	<b>Nine Months Ended March 27, 2020</b>	<b>As a % of Total Revenues</b>
North America	\$ 206,751	50.3%	\$ 631,096	51.0%
Asia-Pacific	141,639	34.4	401,209	32.5
Europe	62,820	15.3	204,418	16.5
Total	<u>\$ 411,210</u>	<u>100.0%</u>	<u>\$ 1,236,723</u>	<u>100.0%</u>

<i>(amount in thousands, except percentages)</i>	<b>Three Months Ended March 29, 2019</b>	<b>As a % of Total Revenues</b>	<b>Nine Months Ended March 29, 2019</b>	<b>As a % of Total Revenues</b>
North America	\$ 195,504	49.0%	\$ 558,028	47.3%
Asia-Pacific	151,263	37.9	469,921	39.9
Europe	52,184	13.1	151,259	12.8
Total	<u>\$ 398,951</u>	<u>100.0%</u>	<u>\$ 1,179,208</u>	<u>100.0%</u>

The following tables set forth our revenues by end market:

<i>(amount in thousands, except percentages)</i>	<b>Three Months Ended March 27, 2020</b>	<b>As a % of Total Revenues</b>	<b>Nine Months Ended March 27, 2020</b>	<b>As a % of Total Revenues</b>
Optical communications	\$ 308,566	75.0%	\$ 933,013	75.4%
Lasers, sensors and other	102,644	25.0	303,710	24.6
Total	<u>\$ 411,210</u>	<u>100.0%</u>	<u>\$ 1,236,723</u>	<u>100.0%</u>

<i>(amount in thousands, except percentages)</i>	<b>Three Months Ended March 29, 2019</b>	<b>As a % of Total Revenues</b>	<b>Nine Months Ended March 29, 2019</b>	<b>As a % of Total Revenues</b>
Optical communications	\$ 298,139	74.7%	\$ 884,454	75.0%
Lasers, sensors and other	100,812	25.3	294,754	25.0
Total	<u>\$ 398,951</u>	<u>100.0%</u>	<u>\$ 1,179,208</u>	<u>100.0%</u>

**4. Earnings per ordinary share**

Basic earnings per ordinary share is computed by dividing reported net income by the weighted-average number of ordinary shares outstanding during each period. Diluted earnings per ordinary share is computed by calculating the effect of potential dilutive ordinary shares outstanding during the period using the treasury stock method. Dilutive ordinary equivalent shares consist of restricted share units and performance share units. Earnings per ordinary share was calculated as follows:

	<u>Three Months Ended</u>		<u>Nine Months Ended</u>	
	<u>March 27, 2020</u>	<u>March 29, 2019</u>	<u>March 27, 2020</u>	<u>March 29, 2019</u>
<i>(amount in thousands except per share amounts)</i>				
Net income attributable to shareholders	<u>\$ 28,267</u>	<u>\$ 28,635</u>	<u>\$ 85,455</u>	<u>\$ 87,998</u>
Weighted-average number of ordinary shares outstanding (thousands of shares)	36,987	36,891	36,970	36,786
Incremental shares arising from the assumed vesting of restricted share units and performance share units (thousands of shares)	<u>810</u>	<u>648</u>	<u>726</u>	<u>597</u>
Weighted-average number of ordinary shares for diluted earnings per ordinary share (thousands of shares)	<u>37,797</u>	<u>37,539</u>	<u>37,696</u>	<u>37,383</u>
Basic earnings per ordinary share	\$ 0.76	\$ 0.78	\$ 2.31	\$ 2.39
Diluted earnings per ordinary share	\$ 0.75	\$ 0.76	\$ 2.27	\$ 2.35
Outstanding performance share units excluded from the computation of diluted earnings per ordinary share (thousands of shares) <sup>(1)</sup>	50	401	50	401

(1) These performance share units were not included in the computation of diluted earnings per ordinary share because they are not expected to vest based on the Company's current assessment of the related performance obligations.

**5. Cash, cash equivalents and short-term investments**

The Company's cash, cash equivalents, and short-term investments by category is as follows:

	<u>Carrying Cost</u>	<u>Unrealized Gain/(Loss)</u>	<u>Fair Value</u>		
			<u>Cash and Cash Equivalents</u>	<u>Marketable Securities</u>	<u>Other Investments</u>
<i>(amount in thousands)</i>					
<b>As of March 27, 2020</b>					
Cash	\$202,610	\$ —	\$ 202,610	\$ —	\$ —
Cash equivalents	21,528	—	21,528	—	—
Liquidity funds	20,954	—	—	—	20,954
Certificates of deposit and time deposits	20,000	—	—	—	20,000
Corporate debt securities	132,877	(1,439)	—	131,438	—
U.S. agency and U.S. Treasury securities	60,497	733	—	61,230	—
Total	<u>\$458,466</u>	<u>\$ (706)</u>	<u>\$ 224,138</u>	<u>\$ 192,668</u>	<u>\$ 40,954</u>
<b>As of June 28, 2019</b>					
Cash	\$178,019	\$ —	\$ 178,019	\$ —	\$ —
Cash equivalents	2,820	—	2,820	—	—
Liquidity funds	20,552	—	—	—	20,552
Certificates of deposit and time deposits	35,028	—	—	—	35,028
Corporate debt securities	130,959	297	—	131,256	—
U.S. agency and U.S. Treasury securities	69,552	105	—	69,657	—
Total	<u>\$436,930</u>	<u>\$ 402</u>	<u>\$ 180,839</u>	<u>\$ 200,913</u>	<u>\$ 55,580</u>



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All highly liquid investments with original maturities of three months or less at the date of purchase are classified as cash equivalents. Management determines the appropriate classification of its investments at the time of purchase and re-evaluates the designations at each balance sheet date. The Company may sell certain of its short-term investments prior to their stated maturities for strategic reasons including, but not limited to, anticipation of credit deterioration and duration management. The maturities of the Company's short-term investments generally range from three months to three years. The Company's short-term investments consist of U.S. Treasuries and fixed income securities and have been classified and accounted for as available-for-sale.

The following table summarizes the cost and estimated fair value of short-term investments classified as available-for-sale securities based on stated effective maturities as of March 27, 2020:

<i>(amount in thousands)</i>	<b>March 27, 2020</b>		<b>June 28, 2019</b>	
	<u>Carrying Cost</u>	<u>Fair Value</u>	<u>Carrying Cost</u>	<u>Fair Value</u>
Due within one year	\$ 30,448	\$ 30,472	\$ 69,746	\$ 69,830
Due between one to five years	162,926	162,196	130,765	131,083
<b>Total</b>	<b>\$ 193,374</b>	<b>\$192,668</b>	<b>\$ 200,511</b>	<b>\$200,913</b>

During the nine months ended March 27, 2020, the Company recognized a realized gain of \$0.1 million from sales and maturities of available-for-sale securities.

As of March 27, 2020, the Company considered the decline in market value of its short-term investments portfolio to be temporary in nature and did not consider any of its securities other-than-temporarily impaired. The Company typically invests in highly-rated securities, and its investment policy generally limits the amount of credit exposure to any one issuer. The policy requires investments generally to be investment grade, with the primary objective of minimizing the potential risk of principal loss. Fair values were determined for each individual security in the investment portfolio. When evaluating an investment for other-than-temporary impairment, the Company reviews factors such as the length of time and extent to which fair value has been below its cost basis, the financial condition of the issuer and any changes thereto, changes in market interest rates, and the Company's intent to sell, or whether it is more likely than not it will be required to sell, the investment before recovery of the investment's cost basis. No impairment losses were recorded for the nine months ended March 27, 2020.

## **6. Fair value of financial instruments**

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. A fair value hierarchy is established, which requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs for the valuation of an asset or liability as of the measurement date. The three levels of inputs that may be used to measure fair value are defined as follows:

Level 1 inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2 inputs are inputs other than quoted prices included within Level 1 that are observable for assets or liabilities, either directly or indirectly. If the assets or liabilities have a specified (contractual) term, Level 2 inputs must be observable for substantially the full term of assets or liabilities.

Level 3 inputs are unobservable inputs for assets or liabilities, which require the reporting entity to develop its own valuation techniques and assumptions.

The Company utilizes the market approach to measure fair value for its financial assets and liabilities. The market approach uses prices and other relevant information generated by market transactions involving identical or comparable assets or liabilities.

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The following table provides details of the financial instruments measured at fair value on a recurring basis, including:

<i>(amount in thousands)</i>	Fair Value Measurements at Reporting Date Using			
	Level 1	Level 2	Level 3	Total
As of March 27, 2020				
<b>Assets</b>				
Cash equivalents	\$ —	\$ 21,528	\$ —	\$ 21,528
Liquidity funds	—	20,954	—	20,954
Certificates of deposit and time deposits	—	20,000	—	20,000
Corporate debt securities	—	131,438	—	131,438
U.S. agency and U.S. Treasury securities	—	61,230	—	61,230
Derivative assets	—	—	—	—
<b>Total</b>	<b>\$ —</b>	<b>\$ 255,150</b>	<b>\$ —</b>	<b>\$ 255,150</b>
<b>Liabilities</b>				
Derivative liabilities	\$ —	\$ 11,977 <sup>(1)</sup>	\$ —	\$ 11,977
<b>Total</b>	<b>\$ —</b>	<b>\$ 11,977</b>	<b>\$ —</b>	<b>\$ 11,977</b>
<i>(amount in thousands)</i>	Fair Value Measurements at Reporting Date Using			
	Level 1	Level 2	Level 3	Total
As of June 28, 2019				
<b>Assets</b>				
Cash equivalents	\$ —	\$ 2,820	\$ —	\$ 2,820
Liquidity funds	—	20,552	—	20,552
Certificates of deposit and time deposits	—	35,028	—	35,028
Corporate debt securities	—	131,256	—	131,256
U.S. agency and U.S. Treasury securities	—	69,657	—	69,657
Derivative assets	—	2,201 <sup>(2)</sup>	—	2,201
<b>Total</b>	<b>\$ —</b>	<b>\$ 261,514</b>	<b>\$ —</b>	<b>\$ 261,514</b>
<b>Liabilities</b>				
Derivative liabilities	\$ —	\$ 2,591 <sup>(3)</sup>	\$ —	\$ 2,591
<b>Total</b>	<b>\$ —</b>	<b>\$ 2,591</b>	<b>\$ —</b>	<b>\$ 2,591</b>

(1) Foreign currency forward and option contracts with a notional amount of \$126.0 million and Canadian dollars of \$0.7 million, and two interest rate swap agreements with an aggregate notional amount of \$125.1 million.

(2) Foreign currency forward contracts with notional amount of \$72.0 million and Canadian dollars of \$0.6 million.

(3) Interest rate swap agreement with a notional amount of \$64.2 million.

### **Derivative financial instruments**

The Company utilizes derivative financial instruments to hedge (i) foreign exchange risk associated with certain foreign currency denominated assets and liabilities and other foreign currency transactions, and (ii) interest rate risk associated with its long-term debt.

The Company minimizes the credit risk associated with its derivative instruments by limiting the exposure to any single counterparty and by entering into derivative instruments only with counterparties that meet the Company's minimum credit quality standard.

***Foreign currency forward and option contracts***

As a result of foreign currency rate fluctuations, the U.S. dollar equivalent values of the Company's foreign currency denominated assets and liabilities fluctuate. The Company uses foreign currency contracts to manage the foreign exchange risk associated with a portion of its foreign currency denominated assets and liabilities and other foreign currency transactions. The Company enters into foreign currency forward and option contracts to hedge fluctuations in the U.S. dollar value of forecasted transactions denominated in Thai baht and Canadian dollars.

The Company may enter into foreign currency forward contracts to hedge fluctuations in the U.S. dollar value of forecasted transactions denominated in Thai baht, including inventory purchases, payroll and other operating expenses. The Company considers these forward contracts as dual-purpose hedges, that hedge both the foreign exchange fluctuation (i) from inception through the forecasted expenditure, and (ii) any subsequent revaluation of the account payable or accrual. The Company may designate the forward contracts that hedge the foreign exchange fluctuation from inception through the forecasted expenditure as cash flow hedges. The gain or loss on a derivative instrument designated and qualifying as a cash flow hedging instrument is recorded as a component of other comprehensive income and reclassified into earnings in the same period or periods during which the hedged forecasted transaction affects earnings. The reclassified amounts are presented in the same income statement line item as the earnings effect of the hedged item. Once the forecasted transactions are recorded, the Company will discontinue the hedging relationship by de-designating the derivative instrument and recording subsequent changes in fair value through contract maturity to foreign exchange gain (loss), net in the unaudited condensed consolidated statements of operations and comprehensive income as a natural hedge against the Thai baht denominated assets and liabilities.

The Company may also enter into non-designated foreign currency forward and option contracts to provide an offset to the re-measurement of foreign currency denominated assets and liabilities and to hedge certain forecasted exposures. Changes in the fair value of these non-designated derivatives are recorded through foreign exchange gain (loss), net in the unaudited condensed consolidated statements of operations and comprehensive income.

As of March 27, 2020, the Company had 100 outstanding U.S. dollar foreign currency forward contracts against Thai baht, with an aggregate notional amount of \$101.0 million and maturity dates ranging from April 2020 through October 2020 that were designated for cash flow hedge accounting. The hedging relationship was determined to be highly effective based on the performance of retrospective and prospective regression testing. During the three and nine months ended March 27, 2020, the Company recorded an unrealized loss of \$6.6 million from changes in the fair value of these foreign currency forward contracts, designated as hedging instruments, in other comprehensive income in the unaudited condensed consolidated statements of operations and comprehensive income. During the three and nine months ended March 27, 2020, the Company de-designated 20 foreign currency forward contracts against the Thai baht that had previously been designated as cash flow hedges and reclassified a loss of \$1.7 million from accumulated other comprehensive income to foreign exchange loss, net, cost of revenues, and selling, general and administrative expenses in the unaudited condensed consolidated statements of operations and comprehensive income. As of March 29, 2019, the Company had no foreign currency forward contracts designated as cash flow hedges.

As of March 27, 2020, the Company had 20 outstanding U.S. dollar foreign currency forward contracts with an aggregate notional amount of \$24.0 million, one outstanding U.S. dollar foreign currency option contract with a notional amount of \$1.0 million, and one outstanding Canadian dollar foreign currency forward contract with a notional amount of \$0.5 million, and maturity dates ranging from June 2020 through July 2020, that were not designated for hedge accounting. These foreign currency option and forward contracts were used to hedge fluctuations in the U.S. dollar value of forecasted transactions denominated in Thai baht and Canadian dollars. During the three and nine months ended March 27, 2020, the Company recorded an unrealized loss of \$2.1 million and \$4.0 million, respectively, from changes in the fair value of these foreign currency option and forward contracts in earnings as foreign exchange loss, net in the unaudited condensed consolidated statements of operations and comprehensive income.

As of March 29, 2019, the Company had 45 outstanding U.S. dollar foreign currency forward contracts with an aggregate notional amount of \$98.0 million, one outstanding U.S. dollar foreign currency option contract with a notional amount of \$5.0 million, and one outstanding Canadian dollar forward contract with a notional amount of \$0.4 million, and maturity dates ranging from April 2019 through August 2019, that were not designated for hedge accounting. These foreign currency forward and option contracts were used to hedge fluctuations in the U.S. dollar value of forecasted transactions denominated in Thai baht and Canadian dollars. During the nine months ended March 29, 2019, the Company recorded an unrealized gain of \$1.5 million from changes in the fair value of these foreign currency forward and option contracts in earnings as foreign exchange loss, net in the unaudited condensed consolidated statements of operations and comprehensive income.

As of March 27, 2020, the amount in accumulated other comprehensive income which is expected to be reclassified into earnings within 12 months is \$4.9 million.

***Interest rate swap agreements***

The Company entered into interest rate swap agreements to mitigate interest rate risk and improve the interest rate profile of the Company's debt obligations. As of March 27, 2020, the Company had two outstanding interest rate swap agreements with an aggregate notional amount of \$125.1 million. As of June 28, 2019, the Company had one outstanding interest rate swap agreement with a notional amount of \$64.2 million.

On July 25, 2018, Fabrinet Thailand entered into an interest rate swap agreement to effectively convert the floating interest rate of its term loan under the Bank of America Credit Facility Agreement to a fixed interest rate of 2.86% per annum through the scheduled maturity of the term loan in June 2023 (see Note 14). The Company did not designate this interest rate swap for hedge accounting.

On September 3, 2019, the Company drew down a term loan under a new Credit Facility Agreement with the Bank of Ayudhya Public Company Limited (the "Bank") (see Note 14) and on September 10, 2019, repaid in full the outstanding term loan under the Bank of America Credit Facility (see Note 14). In conjunction with the funding of the new term loan, the Company entered into a second interest rate swap agreement. The combination of both of these interest rate swaps effectively convert the floating interest rate of the Company's term loan with the Bank to a fixed interest rate of 4.36% per annum through the maturity of the term loan in June 2024.

On September 27, 2019, the Company designated these two interest rate swaps as a cash flow hedge for the Company's term loan under the Credit Facility Agreement with the Bank. The combination of these two interest rate swaps qualified for hedge accounting based on a regression testing result which proved the hedges are highly effective. In addition, the Company has designated and documented contemporaneously the hedging relationships involving these interest rate swaps. At least quarterly, the Company performs a qualitative effectiveness test on the interest rate swaps to support the continued application of hedge accounting. As of March 27, 2020, the hedging relationship was determined to be highly effective based on the performance of a qualitative effectiveness testing. While the Company intends to continue to meet the conditions for hedge accounting, if hedges do not qualify as highly effective, the changes in the fair value of the derivatives used as hedges would be reflected in earnings. From September 27, 2019, any gains or losses related to these interest rate swaps will be recorded in accumulated other comprehensive income in the unaudited condensed consolidated balance sheets, with a portion reclassified from accumulated other comprehensive income into earnings at each reporting period based on either the accrued interest amount or the interest payment.

As of March 27, 2020, the amount in accumulated other comprehensive income that is expected to be reclassified into earnings within 12 months is \$17 thousand.

Prior to September 27, 2019, these interest rate swaps were not designated as cash flow hedges and all changes in the fair value of these interest rate swaps were reflected in earnings. During the nine months ended March 27, 2020 and March 29, 2019, the Company recorded unrealized loss of \$1.7 million and \$1.6 million, respectively, from changes in the fair value of these interest rate swaps as interest expense in the unaudited condensed consolidated statements of operations and comprehensive income.

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The following table provides a summary of the impact of derivative gain (loss) of the Company's foreign currency forward contracts and interest rate swaps which were designated as cash flow hedges on the unaudited condensed consolidated statements of operations and other comprehensive income:

	Financial statements line item	Three Months Ended		Nine Months Ended	
		March 27, 2020	March 29, 2019	March 27, 2020	March 29, 2019
<i>(amount in thousands)</i>					
<b>Derivatives gain (loss) recognized in other comprehensive income:</b>					
Foreign currency forward contracts	Other comprehensive income	\$ (6,609)	\$ —	\$ (6,609)	\$ —
Interest rate swaps	Other comprehensive income	(1,239)	—	(956)	—
<b>Total derivatives loss recognized in other comprehensive income</b>		<u>\$ (7,848)</u>	<u>\$ —</u>	<u>\$ (7,565)</u>	<u>\$ —</u>
<b>Derivatives gain (loss) reclassified from accumulated other comprehensive income into earnings:</b>					
Foreign currency forward contracts	Cost of revenues	\$ 14	\$ —	\$ 14	\$ —
Foreign currency forward contracts	SG&A	1	—	1	—
Foreign currency forward contracts	Foreign exchange loss, net	1,669	—	1,669	—
Interest rate swaps	Interest expense	(405)	—	(838)	—
<b>Total derivatives gain reclassified from accumulated other comprehensive income into earnings</b>		<u>\$ 1,279</u>	<u>\$ —</u>	<u>\$ 846</u>	<u>\$ —</u>
<b>Change in net unrealized loss on derivatives instruments</b>		<u>\$ (6,569)</u>	<u>\$ —</u>	<u>\$ (6,719)</u>	<u>\$ —</u>

### Fair value of derivatives

The following table provides the fair values of the Company's derivative financial instruments for the periods presented:

	March 27, 2020		June 28, 2019	
	Derivative Assets	Derivative Liabilities	Derivative Assets	Derivative Liabilities
<i>(amount in thousands)</i>				
<b>Derivatives not designated as hedging instruments</b>				
Foreign currency forward and option contracts	\$ —	\$ (1,833)	\$ 2,201	\$ —
Interest rate swaps	—	—	—	(2,591)
<b>Derivatives designated as hedging instruments</b>				
Foreign currency forward contracts	\$ 31	\$ (4,956)	\$ —	\$ —
Interest rate swaps	83	(5,302)	—	—
<b>Derivatives, gross balances</b>	<u>\$ 114</u>	<u>\$ (12,091)</u>	<u>\$ 2,201</u>	<u>\$ (2,591)</u>
<b>Derivatives, gross balances offset in the balance sheet</b>	<u>(114)</u>	<u>114</u>	<u>—</u>	<u>—</u>
<b>Derivatives, net balances</b>	<u>\$ —</u>	<u>\$ (11,977)</u>	<u>\$ 2,201</u>	<u>\$ (2,591)</u>

The Company presents its derivatives at net fair values in the unaudited condensed consolidated balance sheets.

The Company's netting arrangements allow net settlements under certain conditions. The Company's derivative instruments are typically settled monthly or quarterly.

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The Company recorded the fair value of derivative financial instruments in the unaudited condensed consolidated balance sheets as follows:

<u>Derivative Financial Instruments</u>	<u>Balance Sheet Line Item</u>
Fair Value of Derivative Assets	Other current assets
Fair Value of Derivative Liabilities	Accrued expenses

### 7. Trade accounts receivable, net

<i>(amount in thousands)</i>	<u>As of March 27, 2020</u>	<u>As of June 28, 2019</u>
Trade accounts receivable	\$283,546	\$ 260,698
Less: allowance for doubtful account	(79)	(96)
Trade accounts receivable, net	<u>\$283,467</u>	<u>\$ 260,602</u>

### 8. Inventories

<i>(amount in thousands)</i>	<u>As of March 27, 2020</u>	<u>As of June 28, 2019</u>
Raw materials	\$ 118,729	\$ 113,321
Work-in-progress	141,646	141,730
Finished goods	18,779	24,916
Goods in transit	11,054	13,645
Inventories	<u>\$290,208</u>	<u>\$ 293,612</u>

### 9. Other receivable

On October 1, 2019, the Company provided funds in the amount of \$24.3 million to a customer to support the customer's transfer of certain manufacturing operations from Berlin, Germany to the Company's facilities in Thailand. The customer has agreed to repay this amount by September 30, 2020. As of March 27, 2020, the Company recorded the \$24.3 million funds as other receivable in the unaudited condensed consolidated balance sheet. For the nine months ended March 27, 2020, the Company classified these funds as an investing activity in the unaudited condensed consolidated statement of cash flows.

### 10. Restricted cash

As of March 27, 2020 and June 28, 2019, the Company had one outstanding standby letter of credit of 6.0 million Euros, related to the Company's support of a customer's transfer of certain manufacturing operations from Berlin, Germany to the Company's facilities in Thailand. As of March 27, 2020 and June 28, 2019, the standby letter of credit was backed by cash collateral of \$7.4 million.

### 11. Leases

The Company leases facilities under non-cancelable operating lease agreements. The Company leases a portion of its capital equipment and vehicles, certain land and buildings for its facilities in Thailand, the Cayman Islands, China, the United States, the United Kingdom and Israel under operating lease arrangements that expire at various dates through 2025. Certain of these lease arrangements provide the Company the ability to extend the lease from one to five years following the expiration of the current term. However, the Company has excluded all lease extension options from its ROU assets and lease liabilities as the Company is not reasonably assured that it will exercise these options. None of the lease agreements contain residual value guarantees provided by the lessee. The Company also has one intercompany lease transaction which is a lease of office and manufacturing space between Fabritek and Fabrinet West.

**Operating leases**

The Company determines if an arrangement contains a lease at inception. The Company applies the guidance in ASC 842 to determine whether a contract is, or contains, a lease. A contract is or contains a lease if the contract conveys the right to control the use of identified property, plant, or equipment (an identified asset) for a period of time in exchange for consideration. Operating leases are included in operating lease ROU assets and operating lease liabilities within the Company’s unaudited condensed consolidated balance sheets. The Company rents certain real estate under agreements that are classified as operating leases.

Operating lease ROU assets and operating lease liabilities are recognized based on the present value of the future minimum lease payments over the lease term at commencement date. As most of the Company’s leases do not provide an implicit rate, the Company uses its incremental borrowing rate based on the information available at the lease commencement date in determining the present value of future payments. The operating lease ROU assets also include any lease payments made and exclude lease incentives and initial direct costs incurred. Variable lease payments are expensed as incurred and are not included within the ROU asset and lease liability calculation. Variable lease payments primarily include reimbursements of costs incurred by lessors for common area maintenance and utilities. The Company’s lease terms may include options to extend or terminate the lease when it is reasonably certain that the Company will exercise that option.

Leases with an initial term of 12 months or less are not recorded on the balance sheet. The Company recognizes lease expense for these leases on a straight-line basis over the lease term. The Company does not account for lease components (e.g., fixed payments including rent) separately from the non-lease components (e.g., common-area maintenance costs).

The following table shows the impact of adoption of ASC 842 on the adoption date of June 29, 2019 on the consolidated balance sheets:

**Consolidated Balance Sheets**

<i>(amount in thousands)</i>	<b>Impact of Adopting ASC 842</b>		
	<b>Balance at June 28, 2019</b>	<b>Adjustment</b>	<b>Balance at June 29, 2019</b>
<b>Assets</b>			
Operating lease ROU assets	\$ —	\$ 5,370	\$ 5,370
<b>Liabilities and Shareholders’ Equity</b>			
Operating lease liabilities, current	\$ —	\$ 1,601	\$ 1,601
Operating lease liabilities, non-current	\$ —	\$ 3,769	\$ 3,769

As of March 27, 2020, the maturities of the Company’s operating lease liabilities were as follows:

<i>(amount in thousands)</i>	
2020 (remaining three months)	\$ 486
2021	2,131
2022	2,000
2023	1,895
2024	878
Thereafter	15
Total undiscounted lease payments	7,405
Less imputed interest	(488)
Total present value of lease liabilities	<u>\$6,917<sup>(1)</sup></u>

<sup>(1)</sup> Includes current portion of operating lease liabilities of \$1.9 million.

Rental expense related to the Company’s operating leases is recognized on a straight-line basis over the lease term. Rental expense for long-term leases for the three and nine months ended March 27, 2020 was \$0.5 million and \$1.5 million, respectively. Rental expense for short-term leases for the three and nine months ended March 27, 2020 and March 29, 2019 was de minimis.

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### **Finance leases**

In connection with the acquisition of Fabrinet UK, the Company assumed the finance lease commitments for certain equipment, with various expiration dates through September 2020. The equipment can be purchased at pre-determined prices upon expiration of such contracts.

As of March 27, 2020, the Company had finance lease liabilities of \$0.2 million, which were recorded under other payables in the unaudited condensed consolidated balance sheets.

The following summarizes additional information related to the Company's operating leases and finance leases:

	<u>As of March 27, 2020</u>
<b>Weighted-average remaining lease term (in years)</b>	
Operating leases	3.7
Finance leases	0.5
<b>Weighted-average discount rate</b>	
Operating leases	3.8%
Finance leases	4.1%

The following information represents supplemental disclosure for the statement of cash flows related to operating and finance leases:

<i>(amount in thousands)</i>	<u>Nine Months Ended March 27, 2020</u>
<b>Cash paid for amounts included in the measurement of lease liabilities</b>	
Operating cash flows from operating leases	\$ 1,794
Financing cash flows from finance leases	\$ 304
ROU assets obtained in exchange for lease liabilities	\$ 7,175
Finance lease assets	\$ 157

## **12. Intangibles**

The following tables present details of the Company's intangibles:

<i>(amount in thousands)</i>	<u>Gross Carrying Amount</u>	<u>Accumulated Amortization</u>	<u>Foreign Currency Translation Adjustment</u>	<u>Net</u>
<b>As of March 27, 2020</b>				
Software	\$ 7,689	\$ (5,365)	\$ —	\$2,324
Customer relationships	4,373	(2,551)	(147)	1,675
Backlog	119	(119)	—	—
<b>Total intangibles</b>	<u>\$ 12,181</u>	<u>\$ (8,035)</u>	<u>\$ (147)</u>	<u>\$3,999</u>

<i>(amount in thousands)</i>	<u>Gross Carrying Amount</u>	<u>Accumulated Amortization</u>	<u>Foreign Currency Translation Adjustment</u>	<u>Net</u>
<b>As of June 28, 2019</b>				
Software	\$ 6,582	\$ (4,868)	\$ —	\$1,714
Customer relationships	4,373	(2,096)	(104)	2,173
Backlog	119	(119)	—	—
<b>Total intangibles</b>	<u>\$ 11,074</u>	<u>\$ (7,083)</u>	<u>\$ (104)</u>	<u>\$3,887</u>



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The Company recorded amortization expense relating to intangibles of \$0.3 million and \$0.3 million for the three months ended March 27, 2020 and March 29, 2019, respectively, and \$0.9 million and \$0.9 million for the nine months ended March 27, 2020 and March 29, 2019, respectively.

The weighted-average remaining life of customer relationships was:

<i>(years)</i>	<u>As of March 27, 2020</u>	<u>As of June 28, 2019</u>
Customer relationships	4.8	5.4

Based on the carrying amount of intangibles as of March 27, 2020, and assuming no future impairment of the underlying assets, the estimated future amortization during each fiscal year was as follows:

<i>(amount in thousands)</i>	
2020 (remaining three months)	\$ 628
2021	1,139
2022	908
2023	650
2024	423
Thereafter	251
<b>Total</b>	<b><u>\$3,999</u></b>

### 13. Goodwill

The changes in the carrying amount of goodwill from the acquisition of Fabrinet UK were as follows:

<i>(amount in thousands)</i>	<u>Goodwill</u>
Balance as of June 28, 2019	\$ 3,705
Foreign currency translation adjustment	(134)
Balance as of March 27, 2020	<b><u>\$ 3,571</u></b>

Goodwill is not deductible for tax purposes. Goodwill is reviewed annually for impairment or more frequently whenever changes or circumstances indicate the carrying amount of goodwill may not be recoverable. During the nine months ended March 27, 2020 and March 29, 2019, there were no goodwill impairment losses.

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### 14. Borrowings

The Company's total borrowings, including current and non-current portions of long-term borrowings, consisted of the following:  
(amount in thousands)

<u>Rate</u>	<u>Conditions</u>	<u>Maturity</u>	<u>As of March 27, 2020</u>	<u>As of June 28, 2019</u>
<b>Long-term borrowings, current portion, net:</b>				
Long-term borrowings, current portion			\$ 12,188	\$ 3,250
Less: Unamortized debt issuance costs – current portion			(32)	—
Long-term borrowings, current portion, net			<u>\$ 12,156</u>	<u>\$ 3,250</u>
<b>Long-term borrowings, non-current portion, net:</b>				
<i>Term loan borrowings:</i>				
1-month LIBOR +1.50% per annum <sup>(1)</sup>	Repayable in quarterly installments	June 2023	\$ —	\$60,938
3-month LIBOR +1.35% per annum <sup>(1)</sup>	Repayable in quarterly installments	June 2024	54,844	—
Less: Current portion			(12,188)	(3,250)
Less: Unamortized debt issuance costs – non-current portion			(103)	—
Long-term borrowings, non-current portion, net			<u>\$ 42,553</u>	<u>\$57,688</u>

<sup>(1)</sup> We have entered into interest rate swaps that effectively fix a series of our future interest payments on our term loans. Refer to Note 6.

The movements of long-term borrowings for the nine months ended March 27, 2020 and March 29, 2019 were as follows:

<i>(amount in thousands)</i>	<u>Nine Months Ended</u>	
	<u>March 27, 2020</u>	<u>March 29, 2019</u>
Opening balance	\$ 60,938	\$ 64,188
Borrowings during the period	60,938	—
Repayments during the period	(67,032)	(2,438)
Closing balance	<u>\$ 54,844</u>	<u>\$ 61,750</u>

As of March 27, 2020, future maturities of long-term borrowings during each fiscal year were as follows:

<i>(amount in thousands)</i>	
2020 (remaining three months)	\$ 3,046
2021	12,188
2022	15,234
2023	12,188
2024	12,188
Total	<u>\$54,844</u>

#### **Credit facility agreements:**

##### *Bank of Ayudhya Public Company Limited*

On August 20, 2019, Fabrinet Thailand (the “Borrower”) and Bank of Ayudhya Public Company Limited (the “Bank”) entered into a Credit Facility Agreement (the “Credit Facility Agreement”). The Credit Facility Agreement provides for a facility of 110.0 million Thai baht (approximately \$3.6 million based on the applicable exchange rate as of September 27, 2019) and \$160.9 million which may be used for, among other things, an overdraft facility, short-term loans against promissory notes, a letter of guarantee facility, a term loan facility and foreign exchange facilities.

The Bank may approve any request for extension of credit under the Credit Facility Agreement and may increase or decrease any facility amount in its sole discretion.

Under the Credit Facility Agreement, on August 20, 2019, the Borrower and the Bank entered into a Term Loan Agreement pursuant to which the Borrower drew down on September 3, 2019 a term loan in the original principal amount of \$60.9 million. The proceeds from the term loan, together with cash on hand, were used to repay outstanding obligations under the Company's previous credit facility agreement with Bank of America, N.A.

The term loan accrues interest at 3-month LIBOR plus 1.35% and is repayable in quarterly installments of \$3.0 million, commencing on September 30, 2019. The term loan will mature on June 30, 2024. The Borrower may prepay the term loan in whole or in part at any time without premium or penalty. Any portion of the term loan repaid or prepaid may not be re-borrowed. During the three and nine months ended March 27, 2020, the Company recorded \$0.5 million and \$1.1 million, respectively, of interest expense in connection with this term loan.

Any borrowings under the Credit Facility Agreement, including those borrowings under the Term Loan Agreement, are guaranteed by Fabrinet and secured by land and buildings owned by the Borrower in the Pathumthani and Chonburi Provinces in Thailand.

The Term Loan Agreement contains affirmative and negative covenants applicable to the Borrower, including delivery of financial statements and other information, compliance with laws, maintenance of insurance, restrictions on granting security interests or liens on its assets, disposing of its assets, incurring indebtedness and making acquisitions. While the term loan is outstanding, the Borrower is required to maintain a loan to value of the mortgaged real property ratio of not greater than 65%. If the loan to value ratio is not maintained, the Borrower will be required to provide additional security or prepay a portion of the term loan in order to restore the required ratio. The Company is also required to maintain a debt service coverage ratio of at least 1.25 times and a debt to equity ratio less than or equal to 1.0 times. In the case of any payment of a dividend by the Company, its debt service coverage ratio must be at least 1.50 times. At March 27, 2020, the Company was in compliance with all of its covenants under the Term Loan Agreement.

The events of default in the Term Loan Agreement include failure to pay amounts due under the Term Loan Agreement or the related finance documents when due, failure to comply with the covenants under the Term Loan Agreement or the related finance documents, cross default with other indebtedness of the Borrower, events of bankruptcy or insolvency in respect of the Borrower, and the occurrence of any event or series of events that in the opinion of the Bank has or is reasonably likely to have a material adverse effect.

At March 27, 2020, there was \$54.8 million outstanding under the term loan.

#### *Bank of America, N.A.*

On May 22, 2014, the Company and a consortium of banks entered into a syndicated senior credit facility agreement led by Bank of America (the "Bank of America Facility Agreement"). The Bank of America Facility Agreement provided for a \$200.0 million credit line, comprised of a \$150.0 million revolving loan facility and a \$50.0 million delayed draw term loan facility.

From time to time, the Company amended the Bank of America Facility Agreement, before repaying all outstanding amounts under the agreement and terminating such agreement on September 10, 2019.

The most recent amendment on June 4, 2018 (i) reduced the revolving commitments thereunder from \$150.0 million to \$25.0 million, (ii) refinanced the outstanding amounts under the revolving loan and term loan facilities into a \$65.0 million term loan which was to be repaid in quarterly installments through the maturity date of June 4, 2023, and (iii) reduced the interest rate margins and commitment fees. The term loan bore interest, at the Company's option, at a rate per annum equal to a LIBOR rate plus a spread of 1.50% to 2.25%, or a base rate plus a spread of 0.50% to 1.25%. During the nine months ended March 27, 2020 and March 29, 2019, the Company recorded \$0.5 million and \$1.8 million, respectively, of interest expense in connection with this term loan.

On September 10, 2019, the Company fully repaid \$61.0 million in principal, accrued interest and other fees under the agreement. The early termination of this agreement did not trigger any early termination fees. At March 27, 2020, there were no amounts outstanding under the Bank of America Facility Agreement. At June 28, 2019, there was \$60.9 million outstanding under the Bank of America Facility Agreement, related to the term loan.

**15. Income taxes**

As of March 27, 2020 and June 28, 2019, the liability for uncertain tax positions including accrued interest and penalties was \$1.5 million and \$2.1 million, respectively. The Company expects the estimated amount of liability associated with its uncertain tax positions to decrease within the next 12 months due to the lapse of the applicable statute of limitations in foreign tax jurisdictions.

The Company files income tax returns in the United States and foreign tax jurisdictions. As of March 27, 2020, the tax years from 2014 through 2017 remain open to examination by U.S. federal and state tax authorities. In addition, tax returns that remain open to examination in Thailand range from the tax years 2015 through 2019, and in the People’s Republic of China and the United Kingdom range from the tax years 2015 through 2018. The Company’s income tax is recognized based on the best estimate of the expected annual effective tax rate for the full financial year of each entity in the Company, adjusted for discrete items arising in that quarter. If the Company’s estimated annual effective tax rate changes, the Company makes a cumulative adjustment in that quarter.

The Company’s effective tax rate for the three months ended March 27, 2020 and March 29, 2019 was 2.4% and 5.2%, respectively, of net income. The decrease was primarily due to the fact that the Company had lower income subject to tax during the three months ended March 27, 2020, compared with the three months ended March 29, 2019.

The Company’s effective tax rate for the nine months ended March 27, 2020 and March 29, 2019 was 4.2% and 5.2%, respectively, of net income. The decrease was primarily due to the fact that the Company had lower income subject to tax during the nine months ended March 27, 2020 as compared to the nine months ended March 29, 2019.

**16. Share-based compensation**

**Share-based compensation**

The grant date fair value of restricted share units and performance share units is based on the market value of our ordinary shares on the date of grant.

The effect of recording share-based compensation expense for the three and nine months ended March 27, 2020 and March 29, 2019 was as follows:

	<u>Three Months Ended</u>		<u>Nine Months Ended</u>	
	<u>March 27, 2020</u>	<u>March 29, 2019</u>	<u>March 27, 2020</u>	<u>March 29, 2019</u>
<i>(amount in thousands)</i>				
<b>Share-based compensation expense by type of award:</b>				
Restricted share units	4,094	3,621	12,678	11,650
Performance share units	2,024	803	5,623	1,723
Total share-based compensation expense	6,118	4,424	18,301	13,373
Tax effect on share-based compensation expense	—	—	—	—
Net effect on share-based compensation expense	<u>\$ 6,118</u>	<u>\$ 4,424</u>	<u>\$ 18,301</u>	<u>\$ 13,373</u>

Share-based compensation expense was recorded in the unaudited condensed consolidated statements of operations and comprehensive income as follows:

	<u>Three Months ended</u>		<u>Nine Months Ended</u>	
	<u>March 27, 2020</u>	<u>March 29, 2019</u>	<u>March 27, 2020</u>	<u>March 29, 2019</u>
<i>(amount in thousands)</i>				
Cost of revenue	\$ 1,489	\$ 1,237	\$ 4,800	\$ 4,384
Selling, general and administrative expense	4,629	3,187	13,501	8,989
Total share-based compensation expense	<u>\$ 6,118</u>	<u>\$ 4,424</u>	<u>\$ 18,301</u>	<u>\$ 13,373</u>

The Company did not capitalize any share-based compensation expense as part of any asset costs during the three and nine months ended March 27, 2020 and March 29, 2019.

***Share-based award activity***

On December 12, 2019, the Company's shareholders approved Fabrinet's 2020 Equity Incentive Plan (the "2020 Plan"). Upon the approval of the 2020 Plan, Fabrinet's Amended and Restated 2010 Performance Incentive Plan (the "2010 Plan") was simultaneously terminated. The 2020 Plan provides for the grant of equity awards thereunder with respect to (i) 1,700,000 ordinary shares, plus (ii) up to 1,300,000 ordinary shares that, as of immediately prior to the termination of the 2010 Plan, had been reserved but not issued pursuant to any awards granted under the 2010 Plan and are not subject to any awards thereunder. Upon termination of the 2010 Plan, 1,281,619 ordinary shares were reserved for issuance under the 2020 Plan pursuant to clause (ii) of the preceding sentence. As of March 27, 2020, there were 30,262 restricted share units outstanding, 3,836 performance share units outstanding and 2,946,847 ordinary shares available for future grant under the 2020 Plan.

As of March 27, 2020, there were 739,838 restricted share units and 436,304 performance share units outstanding under the 2010 Plan. No ordinary shares are available for future grant under the 2010 Plan.

On November 2, 2017, the Company adopted the 2017 Inducement Equity Incentive Plan (the "2017 Inducement Plan") with a reserve of 160,000 ordinary shares authorized for future issuance solely for the granting of inducement share options and equity awards to new employees. The 2017 Inducement Plan was adopted without shareholder approval in reliance on the "employment inducement exemption" provided under the New York Stock Exchange Listed Company Manual. As of March 27, 2020, there were an aggregate of 24,327 restricted share units outstanding and 111,347 ordinary shares available for future grant under the 2017 Inducement Plan.

The 2010 Plan, 2017 Inducement Plan and 2020 Plan are collectively referred to as the "Equity Incentive Plans."

***Restricted share units and performance share units***

Restricted share units and performance share units have been granted under the 2010 Plan, the 2017 Inducement Plan, and the 2020 Plan.

Restricted share units granted to employees generally vest in equal installments over three or four years on each anniversary of the vesting commencement date. Restricted share units granted to non-employee directors generally cliff vest 100% on the first of January, approximately one year from the grant date, provided the director continues to serve through such date.

Performance share units granted to executives will vest, if at all, at the end of a two-year performance period based on the Company's achievement of pre-defined performance criteria, which consist of revenue and non-GAAP gross margin or operating margin targets. The actual number of performance share units that may vest at the end of the performance period ranges from 0% to 100% of the award grant.

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The following table summarizes restricted share unit activity under the Equity Incentive Plans:

	<u>Number of Shares</u>	<u>Weighted- Average Grant Date Fair Value Per Share</u>
Balance as of June 28, 2019	800,751	\$ 42.48
Granted	343,792	\$ 50.32
Issued	(321,659)	\$ 40.82
Forfeited	(28,457)	\$ 42.80
Balance as of March 27, 2020	<u>794,427</u>	\$ 46.54

	<u>Number of Shares</u>	<u>Weighted- Average Grant Date Fair Value Per Share</u>
Balance as of June 29, 2018	1,073,580	\$ 35.19
Granted	341,748	\$ 48.77
Issued	(496,854)	\$ 34.08
Forfeited	(104,194)	\$ 38.50
Balance as of March 29, 2019	<u>814,280</u>	\$ 41.14

The following table summarizes performance share unit activity under the Equity Incentive Plans:

	<u>Number of Shares</u>	<u>Weighted- Average Grant Date Fair Value Per Share</u>
Balance as of June 28, 2019	548,500	\$ 40.97
Granted	242,310	\$ 48.65
Issued	—	—
Forfeited	(350,670)	\$ 36.99
Balance as of March 27, 2020	<u>440,140</u>	\$ 48.37

	<u>Number of Shares</u>	<u>Weighted- Average Grant Date Fair Value Per Share</u>
Balance as of June 29, 2018	605,892	\$ 38.41
Granted	201,994	\$ 48.02
Issued	(227,268)	\$ 40.48
Forfeited	(27,954)	\$ 39.35
Balance as of March 29, 2019	<u>552,664</u>	\$ 41.02

As of March 27, 2020, there was \$15.0 million and \$7.7 million of unrecognized share-based compensation expense related to restricted share units and performance share units, respectively, under the Equity Incentive Plans that is expected to be recorded over a weighted-average period of 2.5 years and 1.3 years, respectively.

For the nine months ended March 27, 2020 and March 29, 2019, the Company withheld an aggregate of 91,481 shares and 231,624 shares, respectively, upon the vesting of restricted share units, based upon the closing share price on the vesting date to settle the employees' minimum statutory obligation for the applicable income and other employment taxes. For the nine months ended March 27, 2020 and March 29, 2019, the Company then remitted cash of \$4.7 million and \$10.4 million, respectively, to the appropriate taxing authorities, and presented it as a financing activity within the unaudited condensed consolidated statements of cash flows. The payment was recorded as a reduction of additional paid-in capital.

**17. Shareholders' equity**

***Share capital***

The Company's authorized share capital is 500,000,000 ordinary shares, par value of \$0.01 per ordinary share, and 5,000,000 preferred shares, par value of \$0.01 per preferred share.

For the three and nine months ended March 27, 2020, the Company issued 52,041 and 230,178 ordinary shares, respectively, upon the vesting of restricted share units, net of shares withheld.

For the three and nine months ended March 29, 2019, the Company issued 78,072 and 492,498 ordinary shares, respectively, upon the vesting of restricted share units, net of shares withheld.

All such issued shares are fully paid.

***Treasury shares***

In August 2017, the Company's board of directors approved a share repurchase program to permit the Company to repurchase up to \$30.0 million worth of its issued and outstanding ordinary shares in the open market in accordance with applicable rules and regulations. In February 2018 and May 2019, the Company's board of directors approved an increase of \$30.0 million and \$50.0 million, respectively, to the original share repurchase authorization, bringing the aggregate authorization to \$110.0 million. During the three and nine months ended March 27, 2020, 355,000 shares were repurchased under the program, at an average price per share of \$58.37, totaling \$20.7 million. As of March 27, 2020, the Company had a remaining authorization to purchase up to \$41.5 million of its ordinary shares under the share repurchase program. Shares repurchased under the share repurchase program are held as treasury shares.

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**18. Accumulated other comprehensive income (loss) (“AOCI”)**

The changes in AOCI for the nine months ended March 27, 2020 and March 29, 2019 were as follows:

<i>(amount in thousands)</i>	<u>Unrealized net (Losses)/Gains on Available-for-sale Securities</u>	<u>Unrealized net (Losses)/Gains on Derivative Instruments</u>	<u>Retirement benefit plan - Prior service cost</u>	<u>Foreign Currency Translation Adjustment</u>	<u>Total</u>
Balance as of June 28, 2019	\$ 952	\$ 32	\$ (2,537)	\$ (833)	\$ (2,386)
Other comprehensive income before reclassification adjustment	(1,310)	(7,565)	478	(353)	(8,750)
Amounts reclassified out of AOCI to the unaudited condensed consolidated statements of operations and comprehensive income	(93)	846	—	—	753
Tax effects	—	—	—	—	—
Other comprehensive income (loss)	<u>\$ (1,403)</u>	<u>\$ (6,719)</u>	<u>\$ 478</u>	<u>\$ (353)</u>	<u>\$ (7,997)</u>
Balance as of March 27, 2020	<u>\$ (451)</u>	<u>\$ (6,687)</u>	<u>\$ (2,059)</u>	<u>\$ (1,186)</u>	<u>\$ (10,383)</u>

<i>(amount in thousands)</i>	<u>Unrealized net (Losses)/Gains on Available-for-sale Securities</u>	<u>Unrealized net (Losses)/Gains on Derivative Instruments</u>	<u>Retirement benefit plan - Prior service cost</u>	<u>Foreign Currency Translation Adjustment</u>	<u>Total</u>
Balance as of June 29, 2018	\$ (1,091)	\$ 33	\$ —	\$ (199)	\$ (1,257)
Other comprehensive income before reclassification adjustment	1,203	—	—	(219)	984
Amounts reclassified out of AOCI to the unaudited condensed consolidated statements of operations and comprehensive income	196	(2)	—	—	194
Tax effects	—	—	—	—	—
Other comprehensive income (loss)	<u>\$ 1,399</u>	<u>\$ (2)</u>	<u>\$ —</u>	<u>\$ (219)</u>	<u>\$ 1,178</u>
Balance as of March 29, 2019	<u>\$ 308</u>	<u>\$ 31</u>	<u>\$ —</u>	<u>\$ (418)</u>	<u>\$ (79)</u>

**19. Commitments and contingencies**

***Letter of credit and Bank guarantees***

As of March 27, 2020 and June 28, 2019, the Company had one outstanding standby letter of credit of 6.0 million Euros, related to the Company’s support of a customer’s transfer of certain manufacturing operations from Berlin, Germany to the Company’s facilities in Thailand. As of March 27, 2020 and June 28, 2019, the standby letter of credit was backed by cash collateral of \$7.4 million.

As of March 27, 2020 and June 28, 2019, there were outstanding bank guarantees given by a bank on behalf of our subsidiary in Thailand for electricity usage and other normal business expenses totaling \$1.5 million and \$1.6 million, respectively, and there were other bank guarantees given by a bank on behalf of our subsidiaries in China and the United Kingdom to support their operations of de minimis amounts.



**Purchase obligations**

Purchase obligations represent legally binding commitments to purchase inventory and other commitments made in the normal course of business to meet operational requirements. Although open purchase orders are considered enforceable and legally binding, their terms generally give the Company the option to cancel, reschedule and/or adjust its requirements based on its business needs prior to the delivery of goods or performance of services. Obligations to purchase inventory and other commitments are generally expected to be fulfilled within one year.

As of March 27, 2020, the Company had purchase obligations to third parties of \$15.2 million.

**Indemnification of directors and officers**

Cayman Islands law does not limit the extent to which a company's memorandum and articles of association may provide for indemnification of directors and officers, except to the extent any such provision may be held by the Cayman Islands courts to be contrary to public policy, such as to provide indemnification against civil fraud or the consequences of committing a crime. Fabrinet's amended and restated memorandum and articles of association provide for indemnification of directors and officers for actions, costs, charges, losses, damages and expenses incurred in their capacities as such, except that such indemnification does not extend to any matter in respect of any fraud or dishonesty that may attach to any of them.

In accordance with Fabrinet's form of indemnification agreement for its directors and officers, Fabrinet has agreed to indemnify its directors and officers against certain liabilities and expenses incurred by such persons in connection with claims by reason of their being such a director or officer. Fabrinet maintains a director and officer liability insurance policy that may enable it to recover a portion of any future amounts paid under the indemnification agreements.

**20. Business segments and geographic information**

Operating segments are defined as components of an enterprise for which separate financial information is available that is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. The Company's chief operating decision maker is Fabrinet's Chief Executive Officer. As of March 27, 2020, the Company operated and internally managed a single operating segment. Accordingly, the Company does not accumulate discrete information with respect to separate product lines and does not have separate reportable segments.

Total revenues are attributed to a particular geographic area based on the bill-to-location of the Company's customers. The Company operates in three geographic regions: North America, Asia-Pacific and Europe.

The following table presents total revenues by geographic region:

<i>(amount in thousands)</i>	<u>Three Months Ended</u>		<u>Nine Months Ended</u>	
	<u>March 27, 2020</u>	<u>March 29, 2019</u>	<u>March 27, 2020</u>	<u>March 29, 2019</u>
North America	\$ 206,751	\$195,504	\$ 631,096	\$ 558,028
Asia-Pacific	141,639	151,263	401,209	469,921
Europe	62,820	52,184	204,418	151,259
	<u>\$ 411,210</u>	<u>\$398,951</u>	<u>\$1,236,723</u>	<u>\$1,179,208</u>

As of March 27, 2020 and March 29, 2019, the Company had approximately \$29.9 million and \$31.7 million, respectively, of long-lived assets based in North America, with the substantial remainder of assets based in Asia-Pacific and Europe.

**Significant customers**

The Company had three and two customers that individually contributed 10% or more of its total trade accounts receivable as of March 27, 2020 and June 28, 2019, respectively.

**21. Subsequent events**

The outbreak of a novel strain of coronavirus (“COVID-19”) was recognized as a pandemic by the World Health Organization on March 11, 2020. The outbreak has spread globally, including to Thailand, the United States, UK and Europe.

The implications of COVID-19 on the Company’s business remain uncertain. Measures taken by governmental authorities and private actors to limit the spread of COVID-19 may interfere with the ability of the Company’s employees, suppliers and other business providers to carry out their assigned tasks or supply materials at ordinary levels of performance. While the Company’s operations are impacted as a result of this pandemic, the Company has not experienced a direct, materially adverse financial impact. The future impact of this pandemic on the Company’s business, financial condition, results of operations and cash flows cannot be predicted. The Company continues to monitor developments with the spread of COVID-19, actions taken by governmental authorities and private actors, and impacts to the Company’s suppliers and customers. The Company continues to work to minimize disruptions to its supply chain and manufacturing capabilities, and to ensure the safety of its employees. While the Company’s operations are impacted as a result of this pandemic, including as a result of restrictions on employees’ ability to travel and requirements that portions of the Company’s workforce work from home, the Company has not experienced a direct, materially adverse financial impact.

The Company is not currently aware of any business interruption or loss contingencies related to COVID-19 that would require recognition in the third quarter of fiscal 2020.

## ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

*In addition to historical information, this Quarterly Report on Form 10-Q contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These statements relate to our expectations, future events or our future financial performance and involve known and unknown risks, uncertainties and other factors that may cause our or our industry's actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements. Forward-looking statements include, but are not limited to, statements about:*

- our goals and strategies;
- our and our customers' estimates regarding future revenues, operating results, expenses, capital requirements and liquidity;
- our belief that we will be able to maintain favorable pricing on our services;
- our expectation that the portion of our revenues attributable to customers in regions outside of North America for the remainder of fiscal year 2020 will be in line with the portion of those revenues for the nine months ended March 27, 2020;
- our expectation that we will incur incremental costs of revenue as a result of our planned expansion of our business into new geographic markets;
- our expectation that our fiscal year 2020 selling, general and administrative ("SG&A") expenses will increase as a percentage of revenue compared to fiscal year 2019 SG&A expenses;
- our expectation that our employee costs will increase in Thailand and the People's Republic of China ("PRC");
- our future capital expenditures and our needs for additional financing;
- the expansion of our manufacturing capacity, including into new geographies;
- the growth rates of our existing markets and potential new markets;
- our ability, and the ability of our customers and suppliers, to respond successfully to technological or industry developments;
- our expectations regarding the potential impact of the COVID-19 pandemic on our business, financial condition and results of operations;
- our suppliers' estimates regarding future costs;
- our ability to increase our penetration of existing markets and to penetrate new markets;
- our plans to diversify our sources of revenues;
- our plans to execute acquisitions;
- trends in the optical communications, industrial lasers, and sensors markets, including trends to outsource the production of components used in those markets;
- our ability to attract and retain a qualified management team and other qualified personnel and advisors; and
- competition in our existing and new markets.

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*These forward-looking statements are subject to certain risks and uncertainties that could cause our actual results to differ materially from those reflected in the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed in this Quarterly Report on Form 10-Q, in particular, the risks discussed under the heading “Risk Factors” in Part II, Item 1A as well as those discussed in other documents we file with the Securities and Exchange Commission. We undertake no obligation to revise or publicly release the results of any revision to these forward-looking statements. Given these risks and uncertainties, readers are cautioned not to place undue reliance on such forward-looking statements. “We,” “us” or “our” collectively refer to Fabrinet and its subsidiaries.*

### **Overview**

We provide advanced optical packaging and precision optical, electro-mechanical and electronic manufacturing services to original equipment manufacturers (“OEMs”) of complex products such as optical communication components, modules and sub-systems, industrial lasers, automotive components, medical devices and sensors. We offer a broad range of advanced optical and electro-mechanical capabilities across the entire manufacturing process, including process design and engineering, supply chain management, manufacturing, complex printed circuit board assembly, advanced packaging, integration, final assembly and testing. Although we focus primarily on low-volume production of a wide variety of high complexity products, which we refer to as “low-volume, high-mix,” we also have the capability to accommodate high-volume production. Based on our experience with, and positive feedback we have received from our customers, we believe we are a global leader in providing these services to the optical communications, industrial lasers and automotive markets.

Our customer base includes companies in complex industries that require advanced precision manufacturing capabilities such as optical communications, industrial lasers, automotive and sensors. The products that we manufacture for our OEM customers include selective switching products; tunable transponders and transceivers; active optical cables; solid state, diode-pumped, gas and fiber lasers; and sensors. In many cases, we are the sole outsourced manufacturing partner used by our customers for the products that we produce for them.

We also design and fabricate application-specific crystals, lenses, prisms, mirrors, laser components, and substrates (collectively referred to as “customized optics”) and other custom and standard borosilicate, clear fused quartz, and synthetic fused silica glass products (collectively referred to as “customized glass”). We incorporate our customized optics and glass into many of the products we manufacture for our OEM customers, and we also sell customized optics and glass in the merchant market.

### **Recent Developments Related to COVID-19**

In the quarter ended March 27, 2020, the effects of the global COVID-19 pandemic impacted us in several ways and created various challenges. It started with our Casix facility in Fuzhou, China, which manufactures custom optics components for us and other customers. In January 2020, while many factories (including our Casix facility) were closed for about eight days because of China’s Lunar New Year holiday, the Chinese government, as part of its efforts to mitigate the spread of COVID-19, ordered that businesses in various parts of the country extend the holiday closures. The Chinese government ordered our Casix facility to not resume operations for almost two weeks. Because of the restrictions on travel in China in place during this period, many of our employees were unable to return from their holiday travel as planned. As a result, fewer than 90% of our employees were able to return to work at our Casix facility until early March. Our other manufacturing facilities also have been affected by various government restrictions put in place in their locations to slow the spread of COVID-19. In Thailand, the government declared a national state of emergency effective March 26, 2020, to reduce the spread of COVID-19. The government required the closure of various businesses, in particular retail establishments, and passed measures restricting movement and activities in Thailand. Our operations in Thailand have not been closed, and we have implemented a number of safety protocols that have allowed our operations in those facilities to continue. Our facilities in the United States, located in California and New Jersey, and in the United Kingdom have remained open, while adhering to the local government restrictions and orders implemented in March 2020, including shelter in place orders and social distancing guidelines, except that our facility in California was closed for about a week beginning in late March until it reopened in early April as a previously classified “essential” business.

The health and well-being of our employees is our top priority. Over the past several months, we have implemented significant precautionary measures throughout our worldwide operations to keep our employees and their families safe, such as mandatory temperature detection at building entrances, rigorous and regular facility and equipment disinfection, and mandatory personal protective equipment protocols, including (1) the wearing of face masks throughout our factories at all times, (2) distributing our employees across shifts to better maintain safe personal distances, (3) isolating incoming parts and materials for a week or more before unpacking, or baking them to kill potential viruses, (4) directing our non-factory personnel to work from home, and (5) restricting all non-employee visits to our campuses.

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During the quarter, we also experienced a shift in the demand for our services, with some customers canceling, decreasing or delaying their orders and other customers accelerating and increasing their orders. However, the most significant effect of COVID-19 on our operations this quarter was the disruption of our supply chain, in which we experienced significant fluctuations in the availability of parts and materials we need to manufacture products for our customers. We were able to mitigate some of these issues by quickly identifying and securing alternative sources; however, these mitigation efforts, combined with our employee safety initiatives, negatively affected our gross margins because they increased our costs and expenses.

Given the unprecedented global, human, and economic impact of COVID-19; the extraordinary economic short-term uncertainty; and the evolving and differing national strategies for dealing with COVID-19, it is extremely difficult and challenging to provide forward-looking disclosure. However, given the uncertainty and concern about the global economy and the health of various industries, we think it important to share some thoughts on how COVID-19 may impact our business in the future:

- With work-from-home protocols in place around the world, global demand for internet bandwidth has grown and we believe it will continue to grow. Because the next-generation telecom and datacom products we manufacture for our customers are important to expand network capacity, we believe this will have a positive impact on our business in the long-term.
- While we believe that the long-term growth outlook for the markets we serve has not been significantly impacted, in the short-term we are likely to continue to see regional downward demand adjustments for products we manufacture for our customers, especially if the COVID-19 outbreak intensifies or returns in various geographic areas as happened at the end of our third fiscal quarter. Moreover, we believe the markets for other products we manufacture, such as the industrial lasers and automotive markets, are likely to see reduced demand in a prolonged economic downturn.
- We expect we will continue to experience disruptions in our supply chain and the availability of parts and materials will continue to fluctuate, especially if the COVID-19 outbreak intensifies or returns in various geographic areas. However, we believe we can mitigate these disruptions by continuing to identify and secure alternative sources.
- A significant portion of our costs are variable and, because of this, we can adjust manufacturing costs relatively quickly to the changing demand of our customers. However, because the largest portion of our costs is for parts and materials, because of the supply chain issues noted above and, to a lesser extent, our commitment to the safety and health protocols we have implemented across our global operations, our gross margins will continue to be negatively affected for the foreseeable future, at least into the first half of fiscal 2021.
- The safety and health of our employees is and will remain a key priority, and we will continue to follow robust safety protocols in all of our facilities.
- Given our \$457.8 million in cash, cash equivalents and short-term investments, and our total debt of approximately \$54.8 million, as of March 27, 2020, we believe we are in a solid position from a capital and financial resources perspective.

## **Revenues**

We believe our ability to expand our relationships with existing customers and attract new customers is due to a number of factors, including our broad range of complex engineering and manufacturing service offerings, flexible low-cost manufacturing platform, process optimization capabilities, advanced supply chain management, excellent customer service, and experienced management team. Although we expect the prices we charge for our manufactured products to decrease over time (partly as a result of competitive market forces), we still believe we will be able to maintain favorable pricing for our services because of our ability to reduce cycle time, adjust our product mix by focusing on more complicated products, improve product quality and yields, and reduce material costs for the products we manufacture. We believe these capabilities have enabled us to help our OEM customers reduce their manufacturing costs while maintaining or improving the design, quality, reliability, and delivery times for their products.

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### **Revenues by Geography**

We generate revenues from three geographic regions: North America, Asia-Pacific and Europe. Revenues are attributed to a particular geographic area based on the bill-to location of our customers, notwithstanding that our customers may ultimately ship their products to end customers in a different geographic region. The majority of our revenues are derived from our manufacturing facilities in Asia-Pacific.

The percentage of our revenues generated from a bill-to location outside of North America decreased from 51.0% in the three months ended March 29, 2019 to 49.7% in the three months ended March 27, 2020 and from 52.7% in the nine months ended March 29, 2019 to 49.0% in the nine months ended March 27, 2020, primarily because the increase in sales to our customers in North America was higher than the increase in sales to our customers outside of North America. Based on the short and medium-term indications and forecasts from our customers, we expect that the portion of our future revenues attributable to customers in regions outside North America for the remainder of fiscal year 2020 will be in line with the portion of total revenues attributable to such customers during the nine months ended March 27, 2020.

The following table presents percentages of total revenues by geographic region:

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>March 27, 2020</b>	<b>March 29, 2019</b>	<b>March 27, 2020</b>	<b>March 29, 2019</b>
North America	50.3%	49.0%	51.0%	47.3%
Asia-Pacific	34.4	37.9	32.5	39.9
Europe	15.3	13.1	16.5	12.8
	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>	<u>100.0%</u>

### **Our Contracts**

We enter into supply agreements with our customers which generally have an initial term of up to three years, subject to automatic renewals for subsequent one-year terms unless expressly terminated. Although there are no minimum purchase requirements in our supply agreements, our customers provide us with rolling forecasts of their demand requirements. Our supply agreements generally include provisions for pricing and periodic review of pricing, consignment of our customer's unique production equipment to us, and the sharing of benefits from cost-savings derived from our efforts. We are generally required to purchase materials, which may include long lead-time materials and materials that are subject to minimum order quantities and/or non-cancelable or non-returnable terms, to meet the stated demands of our customers. After procuring materials, we manufacture products for our customers based on purchase orders that contain terms regarding product quantities, delivery locations and delivery dates. Our customers generally are obligated to purchase finished goods that we have manufactured according to their demand requirements. Materials that are not consumed by our customers within a specified period of time, or are no longer required due to a product's cancellation or end-of-life, are typically designated as excess or obsolete inventory under our contracts. Once materials are designated as either excess or obsolete inventory, our customers are typically required to purchase such inventory from us even if they have chosen to cancel production of the related products. The excess or obsolete inventory is shipped to the customer and revenue is recognized upon shipment.

### **Cost of Revenues**

The key components of our cost of revenues are material costs, employee costs, and infrastructure-related costs. Material costs generally represent the majority of our cost of revenues. Several of the materials we require to manufacture products for our customers are customized for their products and often sourced from a single supplier or in some cases, our own subsidiaries. Shortages from sole-source suppliers due to yield loss, quality concerns and capacity constraints, among other factors, may increase our expenses and negatively impact our gross profit margin or total revenues in a given quarter. Material costs include scrap material. Historically, scrap rate diminishes during a product's life cycle due to process, fixturing and test improvement and optimization.

A second significant element of our cost of revenues is employee costs, including indirect employee costs related to design, configuration and optimization of manufacturing processes for our customers, quality testing, materials testing and other engineering services; and direct costs related to our manufacturing employees. Direct employee costs include employee salaries, insurance and benefits, merit-based bonuses, recruitment, training and retention. Historically, our employee costs have increased primarily due to increases in the number of employees necessary to support our growth and, to a lesser extent, costs to recruit, train and retain employees. Our cost of revenues is significantly impacted by salary levels in Thailand, the PRC and the United Kingdom, the fluctuation of the Thai baht, Chinese Renminbi ("RMB") and

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Pound Sterling (“GBP”) against our functional currency, the U.S. dollar, and our ability to retain our employees. We expect our employee costs to increase as wages continue to increase in Thailand and the PRC. Wage increases may impact our ability to sustain our competitive advantage and may reduce our profit margin. We seek to mitigate these cost increases through improvements in employee productivity, employee retention and asset utilization.

Our infrastructure costs are comprised of depreciation, utilities, facilities management and overhead costs. Most of our facility leases are long-term agreements. Our depreciation costs include buildings and fixed assets, primarily at our Pinehurst and Chonburi campuses in Thailand, and capital equipment located at each of our manufacturing locations.

We expect to incur incremental costs of revenue as a result of our planned expansion into new geographic markets, though we are not able to determine the amount of these incremental expenses.

### **Selling, General and Administrative Expenses**

Our SG&A expenses primarily consist of corporate employee costs for sales and marketing, general and administrative and other support personnel, including research and development expenses related to the design of customized optics and glass, travel expenses, legal and other professional fees, share-based compensation expense and other general expenses not related to cost of revenues. In fiscal year 2020, we expect our SG&A expenses will increase as a percentage of revenue compared with our fiscal year 2019 SG&A expenses.

The compensation committee of our board of directors approved a fiscal year 2020 executive incentive plan with quantitative objectives that are based solely on achieving certain revenue targets and non-GAAP operating margin targets for our fiscal year ending June 26, 2020. Bonuses under the fiscal year 2020 executive incentive plan are payable after the end of fiscal year 2020. In fiscal year 2019, the compensation committee of our board of directors approved a fiscal year 2019 executive incentive plan with quantitative objectives based solely on achieving certain revenue targets and non-GAAP gross margin targets for fiscal year 2019.

### **Additional Financial Disclosures**

#### ***Foreign Exchange***

As a result of our international operations, we are exposed to foreign exchange risk arising from various currency exposures primarily with respect to the Thai baht. Although a majority of our total revenues is denominated in U.S. dollars, a substantial portion of our payroll plus certain other operating expenses are incurred and paid in Thai baht. The exchange rate between the Thai baht and the U.S. dollar has fluctuated substantially in recent years and may continue to fluctuate substantially in the future. We report our financial results in U.S. dollars and our results of operations have been and could in the future be negatively impacted if the Thai baht appreciates against the U.S. dollar. Smaller portions of our expenses are incurred in a variety of other currencies, including RMB, GBP, Canadian dollars, Euros, and Japanese yen, the appreciation of which may also negatively impact our financial results.

In order to manage the risks arising from fluctuations in foreign currency exchange rates, we use derivative instruments. We may enter into foreign exchange currency forward or put option contracts to manage foreign currency exposures associated with certain assets and liabilities and other forecasted foreign currency transactions and may designate these instruments as hedging instruments. The forward and put option contracts generally have maturities of up to 12 months. All foreign currency exchange contracts are recognized in the unaudited condensed consolidated balance sheets at fair value. Gains or losses on our forward and put option contracts generally offset the assets, liabilities, and transactions economically hedged.

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We had foreign currency denominated assets and liabilities in Thai baht, RMB and GBP as follows:

(amount in thousands, except percentages)

	As of March 27, 2020			As of June 28, 2019		
	Currency	\$	%	Currency	\$	%
<b>Assets</b>						
Thai baht	885,394	\$27,277	44.2	664,860	\$21,628	60.0
RMB	189,575	26,918	43.6	53,393	7,767	21.5
GBP	6,171	7,541	12.2	5,270	6,682	18.5
Total		<u>\$61,736</u>	<u>100.0</u>		<u>\$36,077</u>	<u>100.0</u>
<b>Liabilities</b>						
Thai baht	2,047,689	\$63,084	88.4	1,961,972	\$63,825	90.0
RMB	37,561	5,333	7.5	26,373	3,836	5.4
GBP	2,397	2,929	4.1	2,598	3,294	4.6
Total		<u>\$71,346</u>	<u>100.0</u>		<u>\$70,955</u>	<u>100.0</u>

The Thai baht assets represent cash and cash equivalents, trade accounts receivable, deposits and other current assets. The Thai baht liabilities represent trade accounts payable, accrued expenses, income tax payable and other payables. We manage our exposure to fluctuations in foreign exchange rates by the use of foreign currency contracts and offsetting assets and liabilities denominated in the same currency in accordance with management's policy. As of March 27, 2020 there was \$126.0 million of foreign currency forward contracts outstanding on the Thai baht payables. As of June 28, 2019, there was \$72.0 million of foreign currency forward contracts outstanding on the Thai baht payables.

The RMB assets represent cash and cash equivalents, trade accounts receivable and other current assets. The RMB liabilities represent trade accounts payable, accrued expenses, income tax payable and other payables. As of March 27, 2020 and June 28, 2019, we did not have any derivative contracts denominated in RMB.

The GBP assets represent cash, trade accounts receivable, and other current assets. The GBP liabilities represent trade accounts payable and other payables. As of March 27, 2020 and June 28, 2019, we did not have any derivative contracts denominated in GBP.

### Currency Regulation and Dividend Distribution

Foreign exchange regulation in the PRC is primarily governed by the following rules:

- Foreign Currency Administration Rules, as amended on August 5, 2008, or the Exchange Rules;
- Administration Rules of the Settlement, Sale and Payment of Foreign Exchange (1996), or the Administration Rules; and
- Notice on Perfecting Practices Concerning Foreign Exchange Settlement Regarding the Capital Contribution by Foreign-invested Enterprises, as promulgated by the State Administration of Foreign Exchange ("SAFE"), on August 29, 2008, or Circular 142.

Under the Exchange Rules, RMB is freely convertible into foreign currencies for current account items, including the distribution of dividends, interest payments, trade and service-related foreign exchange transactions. However, conversion of RMB for capital account items, such as direct investments, loans, security investments and repatriation of investments, is still subject to the approval of SAFE.

Under the Administration Rules, foreign-invested enterprises may only buy, sell, or remit foreign currencies at banks authorized to conduct foreign exchange business after providing valid commercial documents and relevant supporting documents and, in the case of capital account item transactions, obtaining approval from SAFE. Capital investments by foreign-invested enterprises outside of the PRC are also subject to limitations, which include approvals by the Ministry of Commerce, SAFE and the State Development and Reform Commission.

Circular 142 regulates the conversion by a foreign-invested company of foreign currency into RMB by restricting how the converted RMB may be used. Circular 142 requires that the registered capital of a foreign-invested enterprise settled in RMB converted from foreign currencies may only be used for purposes within the business scope approved by



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the applicable governmental authority and may not be used for equity investments within the PRC. In addition, SAFE strengthened its oversight of the flow and use of the registered capital of foreign-invested enterprises settled in RMB converted from foreign currencies. The use of such RMB capital may not be changed without SAFE's approval and may not be used to repay RMB loans if the proceeds of such loans have not been used.

On January 5, 2007, SAFE promulgated the Detailed Rules for Implementing the Measures for the Administration on Individual Foreign Exchange, or the Implementation Rules. Under the Implementation Rules, PRC citizens who are granted share options by an overseas publicly-listed company are required, through a PRC agent or PRC subsidiary of such overseas publicly-listed company, to register with SAFE and complete certain other procedures.

In addition, the General Administration of Taxation has issued circulars concerning employee share options. Under these circulars, our employees working in the PRC who exercise share options will be subject to PRC individual income tax. Our PRC subsidiary has obligations to file documents related to employee share options with relevant tax authorities and withhold individual income taxes of those employees who exercise their share options.

Furthermore, our transfer of funds to our subsidiaries in Thailand and the PRC are each subject to approval by governmental authorities in case of an increase in registered capital, or subject to registration with governmental authorities in case of a shareholder loan. These limitations on the flow of funds between our subsidiaries and us could restrict our ability to act in response to changing market conditions.

### **Income Tax**

Our effective tax rate is a function of the mix of tax rates in the various jurisdictions in which we do business. We are domiciled in the Cayman Islands. Under the current laws of the Cayman Islands, we are not subject to tax in the Cayman Islands on income or capital gains until March 6, 2039.

Throughout the period of our operations in Thailand, we have generally received income tax and other incentives from the Thailand Board of Investment. Preferential tax treatment from the Thai government in the form of a corporate tax exemption is currently available to us through June 2020 and June 2026 on income generated from projects to manufacture certain products at our Pinehurst campus and Chonburi campus, respectively. Such preferential tax treatment is contingent on various factors, including the export of our customers' products out of Thailand and our agreement not to move our manufacturing facilities out of our current province in Thailand for at least 15 years from the date on which preferential tax treatment was granted (i.e., at least until June 2020 in the case of our Pinehurst campus and until June 2026 in the case of our Chonburi campus). Currently, the corporate income tax rate for our Thai subsidiary is 20%.

The Tax Cuts and Jobs Act ("Tax Reform Act") was enacted on December 22, 2017 and provided for significant changes to U.S. tax law. Among other provisions, the Tax Reform Act reduced the U.S. corporate income tax rate to 21%, which is the current rate for our U.S. subsidiaries.

### **Critical Accounting Policies and Use of Estimates**

We prepare our unaudited condensed consolidated financial statements in conformity with U.S. GAAP, which requires us to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent liabilities on the date of the unaudited condensed consolidated financial statements and the reported amounts of revenues and expenses during the financial reporting period. We continually evaluate these estimates and assumptions based on the most recently available information, our own historical experience and on various other assumptions that we believe to be reasonable under the circumstances, the results form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Because the use of estimates is an integral component of the financial reporting process, actual results could differ from those estimates. Some of our accounting policies require higher degrees of judgment than others in their application. We consider the policies discussed below to be critical to an understanding of our unaudited condensed consolidated financial statements, as their application places the most significant demands on our management's judgment.

Our critical accounting policies are disclosed in our Annual Report on Form 10-K for the fiscal year ended June 28, 2019. The adoption of new accounting policies and accounting standards are disclosed in Note 2 of Notes to Unaudited Condensed Consolidated Financial Statements in Part I, Item 1 of this Quarterly Report on Form 10-Q. There were no changes to our accounting policies other than the adoption of Leases (Topic 842) and Derivatives and Hedging (Topic 815).

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### Results of Operations

The following table sets forth a summary of our unaudited condensed consolidated statements of operations and comprehensive income. Note that period-to-period comparisons of operating results should not be relied upon as indicative of future performance.

<i>(amount in thousands)</i>	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>March 27, 2020</b>	<b>March 29, 2019</b>	<b>March 27, 2020</b>	<b>March 29, 2019</b>
Revenues	\$ 411,210	\$ 398,951	\$ 1,236,723	\$ 1,179,208
Cost of revenues	(366,874)	(352,193)	(1,097,242)	(1,046,610)
Gross profit	44,336	46,758	139,481	132,598
Selling, general and administrative expenses	(17,111)	(14,132)	(50,189)	(41,296)
Expenses related to reduction in workforce	—	(323)	(16)	(727)
Operating income	27,225	32,303	89,276	90,575
Interest income	2,042	2,144	6,080	4,770
Interest expense	(238)	(1,423)	(2,812)	(3,673)
Foreign exchange loss, net	(8)	(3,055)	(2,949)	(408)
Other income, net	203	159	977	798
Income before income taxes	29,224	30,128	90,572	92,062
Income tax expense	(957)	(1,493)	(5,117)	(4,064)
Net income	28,267	28,635	85,455	87,998
Other comprehensive (loss) income, net of tax	(8,231)	998	(7,997)	1,178
Net comprehensive income	<u>\$ 20,036</u>	<u>\$ 29,633</u>	<u>\$ 77,458</u>	<u>\$ 89,176</u>

The following table sets forth a summary of our unaudited condensed consolidated statements of operations and comprehensive income as a percentage of total revenues for the periods indicated.

	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>March 27, 2020</b>	<b>March 29, 2019</b>	<b>March 27, 2020</b>	<b>March 29, 2019</b>
Revenues	100.0%	100.0%	100.0%	100.0%
Cost of revenues	(89.2)	(88.3)	(88.7)	(88.8)
Gross profit	10.8	11.7	11.3	11.2
Selling, general and administrative expenses	(4.2)	(3.5)	(4.1)	(3.5)
Expenses related to reduction in workforce	—	(0.1)	(0.0)	(0.1)
Operating income	6.6	8.1	7.2	7.6
Interest income	0.5	0.5	0.5	0.4
Interest expense	(0.0)	(0.4)	(0.2)	(0.3)
Foreign exchange loss, net	(0.0)	(0.8)	(0.2)	(0.0)
Other income, net	0.0	0.1	0.0	0.1
Income before income taxes	7.1	7.5	7.3	7.8
Income tax expense	(0.2)	(0.4)	(0.4)	(0.3)
Net income	6.9	7.1	6.9	7.5
Other comprehensive (loss) income, net of tax	(2.0)	0.3	(0.6)	0.1
Net comprehensive income	<u>4.9%</u>	<u>7.4%</u>	<u>6.3%</u>	<u>7.6%</u>

The following table sets forth our revenues by end market for the periods indicated.

<i>(amount in thousands)</i>	<b>Three Months Ended</b>		<b>Nine Months Ended</b>	
	<b>March 27, 2020</b>	<b>March 29, 2019</b>	<b>March 27, 2020</b>	<b>March 29, 2019</b>
Optical communications	\$308,566	\$298,139	\$ 933,013	\$ 884,454
Lasers, sensors and other	102,644	100,812	303,710	294,754
Total	<u>\$411,210</u>	<u>\$398,951</u>	<u>\$1,236,723</u>	<u>\$1,179,208</u>

We operate and internally manage a single operating segment. As such, discrete information with respect to separate product lines and segments is not accumulated.

**Comparison of Three and Nine Months Ended March 27, 2020 with Three and Nine Months Ended March 29, 2019**

*Total revenues.*

Our total revenues increased by \$12.3 million, or 3.1%, to \$411.2 million for the three months ended March 27, 2020, compared with \$399.0 million for the three months ended March 29, 2019. This increase was primarily due to an increase in our customers' demand for both optical and non-optical communications manufacturing services during the three months ended March 27, 2020. Revenues from optical and non-optical communications products increased by \$10.4 million and \$1.8 million, or 3.5% and 1.8%, respectively, for the three months ended March 27, 2020.

Our total revenues increased by \$57.5 million, or 4.9%, to \$1,236.7 million for the nine months ended March 27, 2020, compared with \$1,179.2 million for the nine months ended March 29, 2019. This increase was primarily due to an increase in our customers' demand for both optical and non-optical communications manufacturing services during the nine months ended March 27, 2020. Revenues from optical and non-optical communications products increased by \$48.6 million and \$9.0 million, or 5.5% and 3.0%, respectively, for the nine months ended March 29, 2019.

*Cost of revenues.*

Our cost of revenues increased by \$14.7 million, or 4.2%, to \$366.9 million, or 89.2% of total revenues, for the three months ended March 27, 2020, compared with \$352.2 million, or 88.3% of total revenues, for the three months ended March 29, 2019. This increase in cost of revenues was generally in line with the increase in sales volume, except for an increase in costs due to supply chain disruption resulting from COVID-19.

Our cost of revenues increased by \$50.6 million, or 4.8%, to \$1,097.2 million, or 88.7% of total revenues, for the nine months ended March 27, 2020, compared with \$1,046.6 million, or 88.8% of total revenues, for the nine months ended March 29, 2019. This increase in cost of revenues on an absolute dollar basis was in line with the increase in sales volume.

*Gross profit.*

Our gross profit decreased by \$2.4 million, or 5.2%, to \$44.3 million, or 10.8% of total revenues, for the three months ended March 27, 2020, compared with \$46.8 million, or 11.7% of total revenues, for the three months ended March 29, 2019. The decrease was primarily due to a less favorable product mix and an increase in costs due to supply chain disruption resulting from COVID-19.

Our gross profit increased by \$6.9 million, or 5.2%, to \$139.5 million, or 11.3% of total revenues, for the nine months ended March 27, 2020, compared with \$132.6 million, or 11.2% of total revenues, for the nine months ended March 29, 2019. The increase was primarily due to an increase in revenues and effective cost controls.

*SG&A expenses.*

Our SG&A expenses increased by \$3.0 million, or 21.1%, to \$17.1 million, or 4.2% of total revenues, for the three months ended March 27, 2020, compared with \$14.1 million, or 3.5% of total revenues, for the three months ended March 29, 2019. The increase was primarily due to (1) an increase in share-based compensation expenses of \$1.4 million including \$1.2 million from an increase in performance share-based awards granted in the period and \$0.2 million from an increase in restricted share-based awards granted in the period; (2) an increase in new business start-up costs in our subsidiary of \$0.4 million; (3) an increase in severance liabilities expense of \$0.4 million due to a change in labor protection law in Thailand in May 2019 that increased the required severance payment compensation for employees with 20 years of service from 300 days of wage to 400 days of wage; and (4) an increase in executive and management expenses of \$0.2 million from bonuses and other benefits.

Our SG&A expenses increased by \$8.9 million, or 21.5%, to \$50.2 million, or 4.1% of total revenues, for the nine months ended March 27, 2020, compared with \$41.3 million, or 3.5% of total revenues, for the nine months ended March 29, 2019. The increase was primarily due to (1) an increase in share-based compensation expenses of \$4.5 million including \$3.9 million from an increase in performance share-based awards granted in the period and \$0.6 million from an increase in restricted share-based awards granted in the period; (2) an increase in executive and management expenses of \$2.0 million from bonuses and other benefits; (3) an increase in severance liabilities expense of \$1.0 million due to a change in labor protection law in Thailand in May 2019 that increased the required severance payment compensation for employees with 20 years of service from 300 days of wage to 400 days of wage; and (4) an increase in new business start-up costs in our subsidiary of \$0.9 million.

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### *Operating income.*

Our operating income decreased by \$5.1 million to \$27.2 million, or 6.6% of total revenues, for the three months ended March 27, 2020, compared with \$32.3 million, or 8.1% of total revenues, for the three months ended March 29, 2019. The decrease was primarily due to an increase in SG&A expenses.

Our operating income decreased by \$1.3 million to \$89.3 million, or 7.2% of total revenues, for the nine months ended March 27, 2020, compared with \$90.6 million, or 7.7% of total revenues, for the nine months ended March 29, 2019. The decrease was primarily due to an increase in SG&A expenses.

### *Interest income.*

Our interest income decreased by \$0.1 million, or 4.8%, to \$2.0 million, or 0.5% of total revenues, for the three months ended March 27, 2020, compared with \$2.1 million, or 0.5% of total revenues, for the three months ended March 29, 2019. The decrease was primarily due to a reduction in the weighted average interest rate compared to the same period in the previous year from 2.3% to 1.9%, consistent with global interest rate trends.

Our interest income increased by \$1.3 million, or 27.5%, to \$6.1 million, or 0.5% of total revenues, for the nine months ended March 27, 2020, compared with \$4.8 million, or 0.4% of total revenues, for the nine months ended March 29, 2019. The increase was primarily due to an increase in the average balance of our outstanding cash.

### *Interest expense.*

Our interest expense decreased by \$1.2 million to \$0.2 million for the three months ended March 27, 2020, compared with \$1.4 million for the three months ended March 29, 2019. The decrease was due to the implementation of cash flow hedge on interest rate swaps at September 27, 2019, which resulted in (1) the reduction of interest expense of \$0.7 million from the recognition of an unrealized loss from mark-to-market of interest rate swaps in other comprehensive income instead of in interest expense; and (2) the amortization of the fair value of interest rate swaps as of the hedge inception date of \$0.4 million during the three months ended March 27, 2020 in relation to the application of hedge accounting which results in a decrease in interest expense.

Our interest expense decreased by \$0.9 million to \$2.8 million for the nine months ended March 27, 2020, compared with \$3.7 million for the nine months ended March 29, 2019. The decrease was primarily due to an unrealized loss from mark-to-market of interest rate swaps of \$1.7 million for the three months ended September 27, 2019, before applying cash flow hedge, as compared to an unrealized loss of \$1.6 million for the nine months ended March 29, 2019; offset by the amortization of the fair value of interest rate swaps as of the hedge inception date of \$0.8 million during the nine months ended March 27, 2020 in relation to applying hedge accounting which results in a decrease in interest expense.

### *Foreign exchange loss, net.*

We recorded foreign exchange loss, net of \$8 thousand for the three months ended March 27, 2020, compared with a \$3.1 million loss for the three months ended March 29, 2019. The decrease in foreign exchange loss was mainly due to unrealized gain from revaluation of outstanding Thai baht assets and liabilities of \$3.3 million, offset by an unrealized loss from mark to market forward contracts of \$2.1 million and other foreign exchange losses, net of \$1.2 million for the three months ended March 27, 2020, as compared to an unrealized loss from mark to market forward contracts and revaluation of outstanding Thai baht assets and liabilities of \$2.1 million, and a realized loss from payment and receipts of \$0.6 million for the three months ended March 29, 2019.

We recorded foreign exchange loss, net of \$2.9 million for the nine months ended March 27, 2020, compared with a \$0.4 million loss for the nine months ended March 29, 2019. The increase in foreign exchange loss was due to a realized foreign exchange loss from receipts and payments of \$1.6 million for the nine months ended March 27, 2020 as compared to a \$0.9 million realized foreign exchange gain from receipts and payments for the nine months ended March 29, 2019.

### *Income before income taxes.*

We recorded income before income taxes of \$29.2 million and \$90.6 million for the three and nine months ended March 27, 2020, respectively, compared with \$30.1 million and \$92.1 million for the three and nine months ended March 29, 2019, respectively.

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### *Income tax expense.*

Our provision for income tax reflects an effective tax rate of 2.4% and 5.2% for the three months ended March 27, 2020 and March 29, 2019, respectively. The decrease was primarily due to the fact that we had lower income subject to tax during the three months ended March 27, 2020 as compared to the same period in fiscal year 2019.

Our provision for income tax reflects an effective tax rate of 4.2% and 5.2% for the nine months ended March 27, 2020 and March 29, 2019, respectively. The decrease was primarily due to the fact that we had lower income subject to tax during the nine months ended March 27, 2020 as compared to the same period in fiscal year 2019.

### *Net income.*

We recorded net income of \$28.3 million, or 6.9% of total revenues, for the three months ended March 27, 2020, compared with \$28.6 million, or 7.1% of total revenues, for the three months ended March 29, 2019. The decrease was primarily due to (1) an increase in SG&A expenses of \$3.0 million and (2) a decrease in gross profit of \$2.4 million; partially offset by (1) a decrease in foreign exchange loss of \$3.0 million, (2) a net change in interest income and expense of \$1.1 million; (3) a decrease in income tax expense of \$0.5 million, and (4) a decrease in expenses related to reduction in workforce of \$0.3 million.

We recorded net income of \$85.5 million, or 6.9% of total revenues, for the nine months ended March 27, 2020, compared with \$88.0 million, or 7.5% of total revenues, for the nine months ended March 29, 2019. The decrease was primarily due to (1) a net increase in SG&A expenses of \$8.9 million, (2) a net change in foreign exchange gain (loss) of \$2.5 million, and (3) an increase in income tax expenses of \$1.1 million primarily due to the valuation allowance for deferred tax assets; partially offset by (1) an increase in gross profit of \$6.9 million due to increased revenues and effective cost control, (2) a net change in interest income and expense of \$2.2 million, and (3) a decrease in expenses related to reduction in workforce of \$0.7 million.

### *Other comprehensive (loss) income, net.*

We recorded other comprehensive loss of \$8.2 million, or 2.0% of total revenues, for the three months ended March 27, 2020, compared with other comprehensive income of \$1.0 million, or 0.3% of total revenues, for the three months ended March 29, 2019.

We recorded other comprehensive loss of \$8.0 million, or 0.6% of total revenues, for the nine months ended March 27, 2020, compared with other comprehensive income of \$1.2 million, or 0.1% of total revenues, for the nine months ended March 29, 2019.

## **Liquidity and Capital Resources**

### ***Cash Flows and Working Capital***

We primarily finance our operations through cash flow from operations. As of March 27, 2020 and March 29, 2019, we had cash, cash equivalents, and short-term investments of \$457.8 million and \$408.9 million, respectively, and outstanding debt of \$54.8 million and \$61.8 million, respectively.

Our cash and cash equivalents, which primarily consist of cash on hand, demand deposits, and liquid investments with original maturities of three months or less, are placed with banks and other financial institutions. The weighted-average interest rate on our cash and cash equivalents for each of the three and nine months ended March 27, 2020 was 1.9% and 2.0%, respectively, and for the three and nine months ended March 29, 2019 was 2.3% and 1.9%, respectively.

Our cash investments are made in accordance with an investment policy approved by the audit committee of our board of directors. In general, our investment policy requires that securities purchased be rated A1, P-1, F1 or better. No security may have an effective maturity that exceeds three years. Our investments in fixed income securities are primarily classified as available-for-sale and are recorded at fair value. The cost of securities sold is based on the specific identification method. Unrealized gains and losses on these securities are recorded as other comprehensive income (loss) and are reported as a separate component of shareholders' equity.

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During the nine months ended March 27, 2020, (1) we paid off a term loan of \$60.9 million under our previous Bank of America Facility Agreement, (2) our subsidiaries in Thailand drew down a new term loan of \$60.9 million under a new Credit Facility Agreement with the Bank of Ayudhya Public Company Limited, and (3) we repaid \$6.1 million of the new term loan under the new Credit Facility Agreement. As a result, as of March 27, 2020, we had a long-term borrowing of \$54.8 million under our new Credit Facility Agreement. (See Note 14 for further details.) We anticipate that our internally generated working capital, along with our cash and cash equivalents will be adequate to repay these obligations. To better manage our cash on hand, we held short-term investments of \$233.6 million as of March 27, 2020.

We believe that our current cash and cash equivalents, marketable securities, cash flow from operations, and funds available through our credit facility will be sufficient to meet our working capital and capital expenditure needs for at least the next 12 months. Our ability to sustain our working capital position is subject to a number of risks that we discuss in Part II, Item 1A of this Quarterly Report on Form 10-Q.

We also believe that our current manufacturing capacity is sufficient to meet our anticipated production requirements for at least the next few quarters.

The following table shows our cash flows for the periods indicated:

<i>(amount in thousands)</i>	<b>Nine Months Ended</b>	
	<b>March 27, 2020</b>	<b>March 29, 2019</b>
Net cash provided by operating activities	\$ 104,448	\$ 105,504
Net cash used in investing activities	\$ (28,921)	\$ (79,045)
Net cash used in financing activities	\$ (32,000)	\$ (22,063)
Net increase in cash, cash equivalents and restricted cash	\$ 43,527	\$ 4,396

### *Operating Activities*

Net cash provided by operating activities decreased by \$1.1 million, or 1.0%, to \$104.4 million for the nine months ended March 27, 2020, compared with net cash provided by operating activities of \$105.5 million for the nine months ended March 29, 2019. The change in net cash provided by operating activities was not significant compared to the same period of the previous year.

### *Investing Activities*

Net cash used in investing activities decreased by \$50.1 million, or 63.4%, to \$28.9 million for the nine months ended March 27, 2020, compared with net cash used in investing activities of \$79.0 million for the nine months ended March 29, 2019. This decrease was primarily due to net cash received from short-term investments of \$88.2 million, offset by (1) funds provided to a customer of \$24.3 million to support the customer's transfer of certain manufacturing operations from Berlin, Germany to our facilities in Thailand, which the customer has agreed to repay by September 30, 2020, and (2) an increase in investments in property, plant and equipment and intangibles of \$14.8 million.

### *Financing Activities*

Net cash used in financing activities increased by \$9.9 million, or 45.0%, to \$32.0 million for the nine months ended March 27, 2020, compared with net cash used in financing activities of \$22.1 million for the nine months ended March 29, 2019. This increase was primarily due to (1) an increase in ordinary shares repurchase of \$15.3 million and (2) an increase of \$3.7 million in net repayments of loans to banks. The increase was offset by (1) an increase in withholding tax related to net share settlement of restricted share units of \$5.7 million and (2) the release of restricted cash in connection with a business acquisition of \$3.5 million.

## **Off-Balance Sheet Commitments and Arrangements**

As of March 27, 2020, we had one outstanding standby letter of credit of 6.0 million Euros, which was related to our support of a customer's transfer of certain manufacturing operations from Berlin, Germany to our facilities in Thailand. As of March 27, 2020, the standby letter of credit was backed by cash collateral of \$7.4 million.

## **Recent Accounting Pronouncements**

See Note 2 of Notes to Unaudited Condensed Consolidated Financial Statements in Part I, Item 1 of this Quarterly Report on Form 10-Q for recent accounting pronouncements that could have an effect on us.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

#### *Interest Rate Risk*

We had cash, cash equivalents, and short-term investments totaling \$457.8 million and \$437.3 million as of March 27, 2020 and June 28, 2019, respectively. We have interest rate risk exposure relating to the interest income generated by excess cash invested in highly liquid investments with maturities of three months or less from the original dates of purchase. The cash, cash equivalents, and short-term investments are held for working capital purposes. We have not used derivative financial instruments in our investment portfolio. We have not been exposed nor do we anticipate being exposed to material risks due to changes in market interest rates. Declines in interest rates, however, will reduce future investment income. If overall interest rates had declined by 10 basis points during the nine months ended March 27, 2020 and March 29, 2019, our interest income would have decreased by approximately \$0.3 million in each of the respective periods, assuming consistent investment levels.

We also have interest rate risk exposure in movements in interest rates associated with our interest-bearing liabilities. The interest-bearing liabilities are denominated in U.S. dollars and the interest expense is based on the London Inter-Bank Offered Rate (“LIBOR”), plus an additional margin, depending on the lending institution. If the LIBOR had increased by 100 basis points during the nine months ended March 27, 2020 and March 29, 2019, our interest expense would have increased by approximately \$0.1 million and \$0.2 million, respectively, assuming consistent borrowing levels.

We therefore entered into interest rate swap agreements (the “Swap Agreements”) to manage this risk and increase the profile of the Company’s debt obligation. The terms of the Swap Agreements allow the Company to effectively convert the floating interest rate to a fixed interest rate. This locks the variable in interest expenses associated with our floating rate borrowings and results in fixed interest expenses, which is unsusceptible to market rate increase. We designated the Swap Agreements as a cash flow hedge, and they qualify for hedge accounting because the hedges are highly effective. While we intend to continue to meet the conditions for hedge accounting, if hedges do not qualify as highly effective, the changes in the fair value of the derivatives used as hedges would be reflected in our earnings. From September 27, 2019, any gains or losses related to these outstanding interest rate swaps will be recorded in accumulated other comprehensive income in the unaudited condensed consolidated balance sheets, with subsequent reclassification to interest expense when settled.

We maintain an investment portfolio in a variety of financial instruments, including, but not limited to, U.S. government and agency bonds, corporate obligations, money market funds, asset-backed securities, and other investment-grade securities. The majority of these investments pay a fixed rate of interest. The securities in the investment portfolio are subject to market price risk due to changes in interest rates, perceived issuer creditworthiness, marketability, and other factors. These investments are generally classified as available-for-sale and, consequently, are recorded on our unaudited condensed consolidated balance sheets at fair value with unrealized gains or losses reported as a separate component of shareholders’ equity.

Investments in both fixed-rate and floating-rate interest earning instruments carry a degree of interest rate risk. The fair market values of our fixed-rate securities decline if interest rates rise, while floating-rate securities may produce less income than expected if interest rates fall. Due in part to these factors, our future investment income may be less than we expect because of changes in interest rates, or we may suffer losses in principal if forced to sell securities that have experienced a decline in market value because of changes in interest rates.

#### *Foreign Currency Risk*

As a result of our foreign operations, we have significant expenses, assets and liabilities that are denominated in foreign currencies. Substantially all of our employees and most of our facilities are located in Thailand, the PRC and the United Kingdom. Therefore, a substantial portion of our payroll as well as certain other operating expenses are paid in Thai baht, RMB and GBP. The significant majority of our revenues are denominated in U.S. dollars because our customer contracts generally provide that our customers will pay us in U.S. dollars.

As a consequence, our gross profit margins, operating results, profitability and cash flows are adversely impacted when the dollar depreciates relative to the Thai baht, the GBP or the RMB. We have a particularly significant currency rate exposure to changes in the exchange rate between the Thai baht, the GBP, the RMB and the U.S. dollar. We must translate foreign currency-denominated results of operations, assets and liabilities for our foreign subsidiaries to U.S. dollars in our unaudited condensed consolidated financial statements. Consequently, increases and decreases in the value of the U.S. dollar compared with such foreign currencies will affect our reported results of operations and the value of our assets and liabilities on our unaudited condensed consolidated balance sheets, even if our results of operations or the value



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of those assets and liabilities has not changed in its original currency. These transactions could significantly affect the comparability of our results between financial periods or result in significant changes to the carrying value of our assets, liabilities and shareholders' equity.

We attempt to hedge against these exchange rate risks by entering into derivative instruments that are typically one to eighteen months in duration, leaving us exposed to longer term changes in exchange rates. We designated the foreign currency forward contracts used to hedge fluctuations in the U.S. dollar value of forecasted transactions denominated in Thai baht as cash flow hedges, as they qualified for hedge accounting because the hedges are highly effective. While we intend to continue to meet the conditions for hedge accounting, if hedges do not qualify as highly effective, the changes in the fair value of the derivatives used as hedges would be reflected in our earnings. From March 27, 2020, any gains or losses related to these outstanding foreign currency forward contracts will be recorded in accumulated other comprehensive income in the unaudited condensed consolidated balance sheets, with subsequent reclassification to the same statement of operations and comprehensive income line item as the earnings effect of hedge items when settled. We recorded unrealized loss of \$4.0 million and unrealized gain of \$1.5 million for the nine months ended March 27, 2020 and March 29, 2019, respectively, related to derivatives that are not designated as hedging instruments. As foreign currency exchange rates fluctuate relative to the U.S. dollar, we expect to incur foreign currency translation adjustments and may incur foreign currency exchange losses. For example, a 10% weakening in the U.S. dollar against the Thai baht, the RMB and the GBP would have resulted in a decrease in our net dollar position of approximately \$1.1 million and \$0.4 million as of March 27, 2020 and June 28, 2019, respectively. We cannot give any assurance as to the effect that future changes in foreign currency rates will have on our unaudited condensed consolidated financial position, operating results or cash flows.

### **Credit Risk**

Credit risk refers to our exposures to financial institutions, suppliers and customers that have in the past and may in the future experience financial difficulty, particularly in light of recent conditions in the credit markets and the global economy. As of March 27, 2020, our cash and cash equivalents were held in deposits and highly liquid investment products with maturities of three months or less with banks and other financial institutions having credit ratings of A minus or above. Our short-term investments as of March 27, 2020 are held in various financial institutions with a maturity limit not to exceed three years, and all securities are rated A1, P-1, F1 or better. We continue to monitor our surplus cash and consider investment in corporate and U.S. government debt as well as certain available-for-sale securities in accordance with our investment policy. We generally monitor the financial performance of our suppliers and customers, as well as other factors that may affect their access to capital and liquidity. Presently, we believe that we will not incur material losses due to our exposures to such credit risk.

## **ITEM 4. CONTROLS AND PROCEDURES**

### ***Evaluation of Disclosure Controls and Procedures***

Our management, with the participation of our chief executive officer and chief financial officer, evaluated the effectiveness of our disclosure controls and procedures pursuant to Rule 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934 as of the end of the period covered by this Quarterly Report on Form 10-Q. Based on that evaluation, our chief executive officer and chief financial officer concluded that as of the end of the period covered by this Quarterly Report on Form 10-Q, our disclosure controls and procedures were effective to provide reasonable assurance that information we are required to disclose in reports that we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms, and include controls and procedures designed to ensure that the information required to be disclosed by us in such reports is accumulated and communicated to our management, including our chief executive officer and chief financial officer, as appropriate, to allow timely decisions regarding required disclosures. Management's assessment of the effectiveness of our internal control over financial reporting is expressed at the level of reasonable assurance because a control system, no matter how well designed and operated, can provide only reasonable, but not absolute, assurance that the control system's objectives will be met.

### ***Changes in Internal Control over Financial Reporting***

There were no changes in our internal control over financial reporting during the three months ended March 27, 2020 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.



## **PART II: OTHER INFORMATION**

### **ITEM 1. LEGAL PROCEEDINGS**

From time to time, we may be involved in litigation relating to claims arising in the ordinary course of our business. There are currently no material claims or actions pending or threatened against us.

### **ITEM 1A. RISK FACTORS**

*Investing in our ordinary shares involves a high degree of risk. You should carefully consider the following risks, as well as the other information contained in this Quarterly Report on Form 10-Q, including our unaudited condensed consolidated financial statements and the related notes, before investing in our ordinary shares. The risks and uncertainties described below are not the only ones that we may face. Additional risks and uncertainties of which we are unaware, or that we currently deem immaterial, also may become important factors that affect us or our ordinary shares. If any of the following risks actually occur, they may harm our business, financial condition and operating results. In this event, the market price of our ordinary shares could decline and you could lose some or all of your investment.*

#### **COVID-19 Updates**

The COVID-19 pandemic has adversely affected the global economy, disrupted global supply chains and created significant volatility in the financial markets. In addition, the pandemic has resulted in travel restrictions, business closures and the institution of quarantining and other restrictions on movement in many communities. For the quarter ended March 27, 2020, we experienced a decrease in demand for some of our services and disruption in our supply chain because of the effects of COVID-19, which had a negative impact on our financial results. The extent of the impact of COVID-19 on our future business, financial condition and operating results will depend largely on future developments, including (i) the duration and magnitude of the pandemic; (ii) the measures taken by governmental authorities and private actors to limit the spread of COVID-19; (iii) our ability to continue providing products and services; and (iv) the effect of the pandemic on our customers, all of which are highly uncertain and cannot be predicted. While we have updated our risk factors to reflect risks of which we are aware, this situation is changing rapidly and additional impacts may arise that we are not aware of currently.

#### **Risks Related to Our Business**

***Our sales depend on a small number of customers. A reduction in orders from any of these customers, the loss of any of these customers, or a customer exerting significant pricing and margin pressures on us could harm our business, financial condition and operating results.***

We have depended, and will continue to depend, upon a small number of customers for a significant percentage of our total revenues. During each of the three months ended March 27, 2020 and March 29, 2019, we had one customer that accounted for 16.4% and 19.8% respectively, of our total revenues. During each of the nine months ended March 27, 2020 and March 29, 2019, we had one customer that accounted for 16.4% and 18.6%, respectively, of our total revenues. Dependence on a small number of customers means that a reduction in orders from, a loss of, or other adverse actions by any one of these customers would reduce our revenues and could have a material adverse effect on our business, financial condition and operating results. For example, in the three months ended March 27, 2020, we experienced some order cancellations and delays with respect to certain products that we manufacture for our customers due to COVID 19, which adversely affected our revenue.

Further, our customer concentration increases the concentration of our accounts receivable and our exposure to payment default by any of our key customers. Many of our existing and potential customers have substantial debt burdens, have experienced financial distress or have static or declining revenues, all of which may be exacerbated by the sudden and continuing global economic downturn and uncertainty due to the effects of COVID-19 and subsequent adverse conditions in the credit markets, the impact of the U.S.-China trade dispute, and the impact of Brexit. Certain of our customers have gone out of business, declared bankruptcy, been acquired, or announced their withdrawal from segments of the optics market. We generate significant accounts payable and inventory for the services that we provide to our customers, which could expose us to substantial and potentially unrecoverable costs if we do not receive payment from our customers.

Our reliance on a small number of customers gives our customers substantial purchasing power and leverage in negotiating contracts with us. In addition, although we enter into master supply agreements with our customers, the level of business to be transacted under those agreements is not guaranteed. Instead, we are awarded business under those

agreements on a project-by-project basis. Some of our customers have at times significantly reduced or delayed the volume of manufacturing services that they order from us. If we are unable to maintain our relationships with our existing significant customers, our business, financial condition and operating results could be harmed.

***Consolidation in the markets we serve could harm our business, financial condition and operating results.***

Consolidation in the markets we serve has resulted in a reduction in the number of potential customers for our services. For example, II-VI Incorporated completed its acquisition of Finisar Corporation in September 2019, Cisco entered into an agreement in July 2019 to acquire Acacia Communications, and Lumentum Holdings Inc. completed its acquisition of Oclaro, Inc. in December 2018. In some cases, consolidation among our customers has led to a reduction in demand for our services as customers acquired the capacity to manufacture products in-house.

Consolidation among our customers and their customers will continue to adversely affect our business, financial condition and operating results in several ways. Consolidation among our customers and their customers may result in a smaller number of large customers whose size and purchasing power give them increased leverage that may result in, among other things, decreases in our average selling prices. In addition to pricing pressures, this consolidation may also reduce overall demand for our manufacturing services if customers obtain new capacity to manufacture products in-house or discontinue duplicate or competing product lines in order to streamline operations. If demand for our manufacturing services decreases, our business, financial condition and operating results could be harmed.

***If the optical communications market does not expand as we expect, our business may not grow as fast as we expect, which could adversely impact our business, financial condition and operating results.***

Revenues from the optical communications end market represented 75.4% and 75.0% of our total revenues for the nine months ended March 27, 2020 and March 29, 2019, respectively. Our future success as a provider of precision optical, electro-mechanical and electronic manufacturing services for the optical communications market depends on the continued growth of the optics industry and, in particular, the continued expansion of global information networks, particularly those directly or indirectly dependent upon a fiber optic infrastructure. As part of that growth, we anticipate that demand for voice, video, and other data services delivered over high-speed connections (both wired and wireless) will continue to increase. Without network and bandwidth growth, the need for enhanced communications products would be jeopardized. Currently, demand for network services and for high-speed broadband access, in particular, is increasing but growth may be limited by several factors, including, among others: (1) relative strength or weakness of the global economy or certain countries or regions, (2) an uncertain regulatory environment, and (3) uncertainty regarding long-term sustainable business models as multiple industries, such as the cable, traditional telecommunications, wireless and satellite industries, offer competing content delivery solutions. The optical communications market also has experienced periods of overcapacity, some of which have occurred even during periods of relatively high network usage and bandwidth demands. If the factors described above were to slow, stop or reverse the expansion in the optical communications market, our business, financial condition and operating results would be negatively affected.

***Our quarterly revenues, gross profit margins and operating results have fluctuated significantly and may continue to do so in the future, which may cause the market price of our ordinary shares to decline or be volatile.***

Our quarterly revenues, gross profit margins, and operating results have fluctuated significantly and may continue to fluctuate significantly in the future. For example, any of the risks described in this “Risk Factors” section and, in particular, the following factors, could cause our quarterly and annual revenues, gross profit margins, and operating results to fluctuate from period to period:

- any reduction in customer demand or our ability to fulfill customer orders as a result of disruptions in our supply chain caused by COVID-19;
- our ability to acquire new customers and retain our existing customers by delivering superior quality and customer service;
- the cyclicality of the optical communications market, as well as the industrial lasers, medical and sensors markets;
- competition;
- our ability to achieve favorable pricing for our services;
- the effect of fluctuations in foreign currency exchange rates;
- our ability to manage our headcount and other costs; and
- changes in the relative mix in our revenues.

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Therefore, we believe that quarter-to-quarter comparisons of our operating results may not be useful in predicting our future operating results. You should not rely on our results for one quarter as any indication of our future performance. Quarterly variations in our operations could result in significant volatility in the market price of our ordinary shares.

***If we are unable to continue diversifying our precision optical and electro-mechanical manufacturing services across other markets within the optics industry, such as the semiconductor processing, biotechnology, metrology and material processing markets, or if these markets do not grow as fast as we expect, our business may not grow as fast as we expect, which could adversely impact our business, financial condition and operating results.***

We intend to continue diversifying across other markets within the optics industry, such as the semiconductor processing, biotechnology, metrology, and material processing markets, to reduce our dependence on the optical communications market and to grow our business. Currently, the optical communications market contributes the significant majority of our revenues. There can be no assurance that our efforts to further expand and diversify into other markets within the optics industry will prove successful or that these markets will continue to grow as fast as we expect. In the event that the opportunities presented by these markets prove to be less than anticipated, if we are less successful than expected in diversifying into these markets, or if our margins in these markets prove to be less than expected, our growth may slow or stall, and we may incur costs that are not offset by revenues in these markets, all of which could harm our business, financial condition and operating results.

***We face significant competition in our business. If we are unable to compete successfully against our current and future competitors, our business, financial condition and operating results could be harmed.***

Our current and prospective customers tend to evaluate our capabilities against the merits of their internal manufacturing as well as the capabilities of other third-party manufacturers. We believe the internal manufacturing capabilities of current and prospective customers are our primary competition. This competition is particularly strong when our customers have excess manufacturing capacity, as was the case when the markets that we serve experienced a significant downturn in 2008 and 2009 that resulted in underutilized capacity. Should our existing and potential customers have excess manufacturing capacity at their facilities, it could adversely affect our business. In addition, as a result of the 2011 flooding in Thailand, some of our customers began manufacturing products internally or using other third-party manufacturers that were not affected by the flooding. If our customers choose to manufacture products internally rather than to outsource production to us, or choose to outsource to a third-party manufacturer, our business, financial condition and operating results could be harmed.

Competitors in the market for optical manufacturing services include Benchmark Electronics, Inc., Celestica Inc., Sanmina-SCI Corporation, Jabil Circuit, Inc., and Venture Corporation Limited. Our customized optics and glass operations face competition from companies such as Browave Corporation, Fujian Castech Crystals, Inc., Photop Technologies, Inc., and Research Electro-Optic, Inc. Our UK competitors for printed circuit board assemblies include STI Limited and Axiom Manufacturing Services Limited. Other existing contract manufacturing companies, original design manufacturers or outsourced semiconductor assembly and test companies could also enter our target markets. In addition, we may face more competitors as we attempt to penetrate new markets.

Many of our customers and potential competitors have longer operating histories, greater name recognition, larger customer bases and significantly greater resources than we have. These advantages may allow them to devote greater resources than we can to the development and promotion of service offerings that are similar or superior to our service offerings. These competitors may also engage in more extensive research and development, undertake more far-reaching marketing campaigns, adopt more aggressive pricing policies or offer services that achieve greater market acceptance than ours. These competitors may also compete with us by making more attractive offers to our existing and potential employees, suppliers, and strategic partners. Further, consolidation in the optics industry could lead to larger and more geographically diverse competitors. New and increased competition could result in price reductions for our services, reduced gross profit margins or loss of market share. We may not be able to compete successfully against our current and future competitors, and the competitive pressures we face may harm our business, financial condition and operating results.

***Cancellations, delays or reductions of customer orders and the relatively short-term nature of the commitments of our customers could harm our business, financial condition and operating results.***

We do not typically obtain firm purchase orders or commitments from our customers that extend beyond 13 weeks. While we work closely with our customers to develop forecasts for periods of up to one year, these forecasts are not binding and may be unreliable. Customers may cancel their orders, change production quantities from forecasted volumes or delay production for a number of reasons beyond our control. Any material delay, cancellation or reduction of orders could cause our revenues to decline significantly and could cause us to hold excess materials. Many of our costs and operating expenses are fixed. As a result, a reduction in customer demand could decrease our gross profit and harm our business, financial condition and operating results. For example, in the three months ended March 27, 2020, we experienced some order cancellations and delays with respect to telecom products that we manufacture for our customers due to COVID-19; however, these cancellations and delays were partially offset by increased demand for datacom products.

In addition, we make significant decisions, including production schedules, material procurement commitments, personnel needs and other resource requirements, based on our estimate of our customers' requirements. The short-term nature of our customers' commitments and the possibility of rapid changes in demand for their products reduce our ability to accurately estimate the future requirements of our customers. Inability to forecast the level of customer orders with certainty makes it difficult to allocate resources to specific customers, order appropriate levels of materials and maximize the use of our manufacturing capacity. This could also lead to an inability to meet a spike in production demand, all of which could harm our business, financial condition and operating results.

***Our exposure to financially troubled customers or suppliers could harm our business, financial condition and operating results.***

We provide manufacturing services to companies, and rely on suppliers, that have in the past and may in the future experience financial difficulty, particularly in light of the sudden and continuing global economic downturn and uncertainty due to the effects of COVID-19 and subsequent adverse conditions in the credit markets that have affected access to capital and liquidity. As a result, we devote significant resources to monitor receivables and inventory balances with certain of our customers. If our customers experience financial difficulty, we could have difficulty recovering amounts owed to us from these customers, or demand for our services from these customers could decline. For example, in July 2014, one of our customers filed for bankruptcy protection under the Local Trade Court in France; although the bankruptcy of this customer did not have a significant effect on our consolidated financial statements, the same may not be the case if a significant customer were to file for bankruptcy protection in the future. If our suppliers experience financial difficulty, we could have trouble sourcing materials necessary to fulfill production requirements and meet scheduled shipments. Any such financial difficulty could adversely affect our operating results and financial condition by resulting in a reduction in our revenues, a charge for inventory write-offs, a provision for doubtful accounts, and larger working capital requirements due to increased days in inventory and days in accounts receivable.

***Fluctuations in foreign currency exchange rates and changes in governmental policies regarding foreign currencies could increase our operating costs, which would adversely affect our operating results.***

Volatility in the functional and non-functional currencies of our entities and the U.S. dollar could seriously harm our business, financial condition, and operating results. The primary impact of currency exchange fluctuations is on our cash, receivables, and payables of our operating entities.

Our customer contracts generally require that our customers pay us in U.S. dollars. However, the majority of our payroll and other operating expenses are paid in Thai baht. As a result of these arrangements, we have significant exposure to changes in the exchange rate between the Thai baht and the U.S. dollar, and our operating results are adversely impacted when the U.S. dollar depreciates relative to the Thai baht and other currencies. We have experienced such depreciation in the U.S. dollar as compared with the Thai baht, and our results have been adversely impacted by this fluctuation in exchange rates. As of March 27, 2020, the U.S. dollar had appreciated approximately 3.9% against the Thai baht since March 30, 2018. Further, while we attempt to hedge against certain exchange rate risks, we typically enter into hedging contracts with maturities of up to 12 months, leaving us exposed to longer term changes in exchange rates.

Also, we have significant exposure to changes in the exchange rate between the Chinese Renminbi ("RMB") and pound sterling ("GBP") and the U.S. dollar. The expenses of our subsidiaries located in the PRC and the United Kingdom are denominated in RMB and GBP, respectively. Currently, RMB are convertible in connection with trade- and service-related foreign exchange transactions, foreign debt service, and payment of dividends. The PRC government may at its discretion restrict access in the future to foreign currencies for current account transactions. If this occurs, our PRC subsidiary may not be able to pay us dividends in U.S. dollars without prior approval from the PRC State Administration of Foreign Exchange. In addition, conversion of RMB for most capital account items, including direct investments, is still

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subject to government approval in the PRC. This restriction may limit our ability to invest the earnings of our PRC subsidiary. As of March 27, 2020, the U.S. dollar had appreciated approximately 12.9% against the RMB since March 30, 2018. There remains significant international pressure on the PRC government to adopt a substantially more liberalized currency policy. GBP are convertible in connection with trade- and service-related foreign exchange transactions and foreign debt service. As of March 27, 2020, the U.S. dollar had appreciated approximately 14.9% against the GBP since March 30, 2018. Any appreciation in the value of the RMB and GBP against the U.S. dollar could negatively impact our operating results.

***We purchase some of the critical materials used in certain of our products from a single source or a limited number of suppliers. Supply shortages have in the past, and could in the future, impair the quality, reduce the availability or increase the cost of materials, which could harm our revenues, profitability and customer relations.***

We rely on a single source or a limited number of suppliers for critical materials used in a significant number of the products we manufacture. We generally purchase these single or limited source materials through standard purchase orders and do not maintain long-term supply agreements with our suppliers. We generally use a rolling 12-month forecast based on anticipated product orders, customer forecasts, product order history, backlog, and warranty and service demand to determine our materials requirements. Lead times for the parts and components that we order vary significantly and depend on factors such as manufacturing cycle times, manufacturing yields, and the availability of raw materials used to produce the parts or components. Historically, we have experienced supply shortages resulting from various causes, including reduced yields by our suppliers, which prevented us from manufacturing products for our customers in a timely manner. More recently, for the quarter ended March 27, 2020, we experienced significant fluctuations in the availability of certain materials due to COVID-19, which had an adverse impact on our revenue and costs. Our revenues, profitability and customer relations will be harmed by continued fluctuations in the availability of materials, a stoppage or delay of supply, a substitution of more expensive or less reliable parts, the receipt of defective parts or contaminated materials, an increase in the price of supplies, or an inability to obtain reductions in price from our suppliers in response to competitive pressures.

We continue to undertake programs to strengthen our supply chain. Nevertheless, we are experiencing, and expect for the foreseeable future to continue to experience, strain on our supply chain, and periodic supplier problems. We have incurred, and expect to continue to incur for the foreseeable future, costs to address these problems.

***Managing our inventory is complex and may require write-downs due to excess or obsolete inventory, which could cause our operating results to decrease significantly in a given fiscal period.***

Managing our inventory is complex. We are generally required to procure material based upon the anticipated demand of our customers. The inaccuracy of these forecasts or estimates could result in excess supply or shortages of certain materials. Inventory that is not used or expected to be used as and when planned may become excess or obsolete. Generally, we are unable to use most of the materials purchased for one of our customers to manufacture products for any of our other customers. Additionally, we could experience reduced or delayed product shipments or incur additional inventory write-downs and cancellation charges or penalties, which would increase costs and could harm our business, financial condition and operating results. While our agreements with customers are structured to mitigate our risks related to excess or obsolete inventory, enforcement of these provisions may result in material expense, and delay in payment for inventory. If any of our significant customers becomes unable or unwilling to purchase inventory or does not agree to such contractual provisions in the future, our business, financial condition and operating results may be harmed.

***We conduct operations in a number of countries, which creates logistical and communications challenges for us and exposes us to other risks and challenges that could harm our business, financial condition and operating results.***

The vast majority of our operations, including manufacturing and customer support, are located primarily in the Asia-Pacific region. The distances between Thailand, the PRC and our customers and suppliers globally, create a number of logistical and communications challenges for us, including managing operations across multiple time zones, directing the manufacture and delivery of products across significant distances, coordinating the procurement of raw materials and their delivery to multiple locations and coordinating the activities and decisions of our management team, the members of which are based in different countries.

Our customers are located throughout the world, and our principal manufacturing facilities are located in Thailand. Total revenues from the bill-to-location of customers outside of North America accounted for 49.0% and 52.7% of our total revenues for the nine months ended March 27, 2020 and March 29, 2019, respectively. We expect that total revenues from the bill-to-location of customers outside of North America will continue to account for a significant portion of our total revenues. Our customers also depend on international sales, which further exposes us to the risks associated with international operations. Conducting business outside the United States subjects us to a number of additional risks and challenges, including:

- compliance with a variety of domestic and foreign laws and regulations, including trade regulatory requirements;

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- periodic changes in a specific country's or region's economic conditions, such as recession;
- unanticipated restrictions on our ability to sell to foreign customers where sales of products and the provision of services may require export licenses or are prohibited by government action (for example, in early 2018, the U.S. Department of Commerce prohibited the export and sale of a broad category of U.S. products, as well as the provision of services, to ZTE Corporation, and in 2019, to Huawei, both of which are customers of certain of our customers);
- fluctuations in currency exchange rates;
- inadequate protection of intellectual property rights in some countries; and
- potential political, legal and economic instability, foreign conflicts, and the impact of regional and global infectious illnesses in the countries in which we and our customers and suppliers are located.

Our failure to manage the risks and challenges associated with our international operations could have a material adverse effect on our business.

***We are subject to governmental export and import controls in several jurisdictions that subject us to a variety of risks, including liability, impairment of our ability to compete in international markets, and decreased sales and customer orders.***

We are subject to governmental export and import controls in Thailand, the PRC, the United Kingdom and the United States that may limit our business opportunities. Various countries regulate the import of certain technologies and have enacted laws or taken actions that could limit (1) our ability to export or sell the products we manufacture and (2) our customers' ability to export or sell products that we manufacture for them. The export of certain technologies from the United States, the United Kingdom and other nations to the PRC is barred by applicable export controls, and similar prohibitions could be extended to Thailand, thereby limiting our ability to manufacture certain products. Any change in export or import regulations or related legislation, shift in approach to the enforcement of existing regulations, or change in the countries, persons or technologies targeted by such regulations, could limit our ability to offer our manufacturing services to existing or potential customers, which could harm our business, financial condition and operating results.

For example, in May 2019, the U.S. Commerce Department's Bureau of Industry and Security (BIS) added Huawei and certain affiliates to the BIS Entity List. This action denied Huawei the ability to purchase products, software and technology that are subject to U.S. Export Administration Regulations (EAR). Although we do not sell directly to Huawei, some of our customers do sell to Huawei directly. To ensure compliance, some of our customers immediately suspended shipments to Huawei in order to begin assessments of the products they sold to Huawei (and its affiliates), to determine whether these products were subject to the restrictions resulting from the ban. This had an immediate impact on our customer orders in the fourth quarter of fiscal year 2019, which affected our revenue for the quarter. We expect this ban to continue to adversely affect orders from our customers for the foreseeable future.

***We are subject to risks related to the ongoing U.S.-China trade dispute, including increased tariffs on materials that we use in manufacturing, which could adversely affect our business, financial condition and operating results.***

In August 2019, the U.S. Presidential Administration imposed tariffs on a wide range of products and goods manufactured in China that are directly or indirectly imported into the U.S. Although the U.S. Administration announced on January 15, 2020 the reduction of certain tariffs on Chinese imported goods and delayed certain other related tariffs, we cannot assure you that the U.S. Administration will not continue to increase tariffs on imports from China or alter trade agreements and terms between China and the United States, which may include limiting trade with China. Trade restrictions, including tariffs, quotas, embargoes, safeguards and customs restrictions, could have the effect of increasing the cost of materials we use to manufacture certain products, which could result in lower margins. The tariffs could also result in disruptions to our supply chain, as suppliers struggle to fill orders from companies trying to purchase goods in bulk ahead of announced tariffs. The institution of trade tariffs both globally and between the U.S. and China specifically could also cause a decrease in the sales of our customers' products to end users located in China, which could directly impact our revenues in the form of reduced orders. If existing tariffs are raised further or if new tariffs are imposed on additional categories of components used in our manufacturing activities, and if we are unable to pass the costs of such tariffs on to our customers, our operating results would be harmed.



***Our business and operations would be adversely impacted in the event of a failure of our information technology infrastructure and/or cyber security attacks.***

We rely upon the capacity, availability and security of our information technology hardware and software infrastructure. For instance, we use a combination of standard and customized software platforms to manage, record, and report all aspects of our operations and, in many instances, enable our customers to remotely access certain areas of our databases to monitor yields, inventory positions, work-in-progress status and vendor quality data. We are constantly expanding and updating our information technology infrastructure in response to our changing needs. Any failure to manage, expand and update our information technology infrastructure or any failure in the operation of this infrastructure could harm our business.

Despite our implementation of security measures, our systems are vulnerable to damage caused by computer viruses, natural disasters, unauthorized access and other similar disruptions. Any system failure, accident or security breach could result in disruptions to our operations. To the extent that any disruption, cyber-attack or other security breach results in a loss or damage to our data, or inappropriate disclosure of confidential information, our business could be harmed. In addition, we may be required to incur significant costs to protect against damage caused by these disruptions or security breaches in the future.

***If we fail to adequately expand our manufacturing capacity, we will not be able to grow our business, which would harm our business, financial condition and operating results. Conversely, if we expand too much or too rapidly, we may experience excess capacity, which would harm our business, financial condition and operating results.***

We may not be able to pursue many large customer orders or sustain our historical growth rates if we do not have sufficient manufacturing capacity to enable us to commit to provide customers with specified quantities of products. If our customers do not believe that we have sufficient manufacturing capacity, they may: (1) outsource all of their production to another source that they believe can fulfill all of their production requirements; (2) look to a second source for the manufacture of additional quantities of the products that we currently manufacture for them; (3) manufacture the products themselves; or (4) otherwise decide against using our services for their new products.

Most recently, we expanded our manufacturing capacity by building a new facility in Chonburi, Thailand, which was completed in March 2017. We may continue to devote significant resources to the expansion of our manufacturing capacity, and any such expansion will be expensive, will require management's time and may disrupt our operations. In the event we are unsuccessful in our attempts to expand our manufacturing capacity, our business, financial condition and operating results could be harmed.

However, if we expand our manufacturing capacity and are unable to promptly utilize the additional space due to reduced demand for our services or an inability to win new projects, new customers or penetrate new markets, or if the optics industry does not grow as we expect, we may experience periods of excess capacity, which could harm our business, financial condition and operating results.

***Political unrest and demonstrations, as well as changes in the political, social, business or economic conditions in Thailand, could harm our business, financial condition and operating results.***

The majority of our assets and manufacturing operations are located in Thailand. Therefore, political, social, business and economic conditions in Thailand have a significant effect on our business. In March 2020, Thailand was assessed as a medium political risk by MARSH Political Risk, a risk management, insurance and consulting firm. Any changes to tax regimes, laws, exchange controls or political action in Thailand may harm our business, financial condition and operating results.

Thailand has a history of political unrest that includes the involvement of the military as an active participant in the ruling government. In recent years, political unrest in the country has sparked political demonstrations and, in some instances, violence. In March 2019, Thailand held its first general election since the Thai military took over the government in a coup in May 2014. In June 2019, General Prayut Chan-o-cha was elected as Prime Minister, and in July 2019, the new Prime Minister's nominees for cabinet ministers were appointed. Any future political instability in the Kingdom of Thailand could prevent shipments from entering or leaving the country, disrupt our ability to manufacture products in Thailand, and force us to transfer our operations to more stable, and potentially more costly, regions.

Further, the Thai government may raise the minimum wage standards for labor and could repeal certain promotional certificates that we have received or tax holidays for certain export and value added taxes that we enjoy, either preventing us from engaging in our current or anticipated activities or subjecting us to higher tax rates. A new regime could nationalize our business or otherwise seize our assets and any other future political instability could harm our business, financial condition and operating results.

***We expect to continue to invest in our manufacturing operations in the PRC, which will continue to expose us to risks inherent in doing business in the PRC, any of which risks could harm our business, financial condition and operating results.***

We anticipate that we will continue to invest in our customized optics manufacturing facilities located in Fuzhou, China. Because these operations are located in the PRC, they are subject to greater political, legal and economic risks than the geographies in which the facilities of many of our competitors and customers are located. In particular, the political and economic climate in the PRC (both at national and regional levels) is fluid and unpredictable. In March 2020, MARSH Political Risk assessed the PRC as a medium political risk. A large part of the PRC's economy is still being operated under varying degrees of control by the PRC government. By imposing industrial policies and other economic measures, such as control of foreign exchange, taxation, import and export tariffs, environmental regulations, land use rights, intellectual property and restrictions on foreign participation in the domestic market of various industries, the PRC government exerts considerable direct and indirect influence on the development of the PRC economy. Many of the economic reforms carried out by the PRC government are unprecedented or experimental and are expected to change further. Any changes to the political, legal or economic climate in the PRC could harm our business, financial condition and operating results.

Our PRC subsidiary is a "wholly foreign-owned enterprise" and is therefore subject to laws and regulations applicable to foreign investment in the PRC, in general, and laws and regulations applicable to wholly foreign-owned enterprises, in particular. The PRC has made significant progress in the promulgation of laws and regulations pertaining to economic matters such as corporate organization and governance, foreign investment, commerce, taxation and trade. However, the promulgation of new laws, changes in existing laws and abrogation of local regulations by national laws may have a negative impact on our business and prospects. In addition, these laws and regulations are relatively new, and published cases are limited in volume and non-binding. Therefore, the interpretation and enforcement of these laws and regulations involve significant uncertainties. Laws may be changed with little or no prior notice, for political or other reasons. These uncertainties could limit the legal protections available to foreign investors. Furthermore, any litigation in the PRC may be protracted and result in substantial costs and diversion of resources and management's attention.

***Natural disasters (like the 2011 flooding in Thailand), epidemics, acts of terrorism and other political and economic developments could harm our business, financial condition and operating results.***

Natural disasters, such as the 2011 flooding in Thailand, where most of our manufacturing operations are located, could severely disrupt our manufacturing operations and increase our supply chain costs. These events, over which we have little or no control, could cause a decrease in demand for our services, make it difficult or impossible for us to manufacture and deliver products or for our suppliers to deliver components allowing us to manufacture those products, require large expenditures to repair or replace our facilities, or create delays and inefficiencies in our supply chain. For example, the 2011 flooding in Thailand forced us to temporarily shut down all of our manufacturing facilities in Thailand and cease production permanently at our Chokchai facility, which adversely affected our ability to meet our customers' demands during fiscal year 2012. In some countries in which we operate, including the PRC, United States and Thailand, outbreaks of infectious diseases such as COVID-19, H1N1 influenza virus, severe acute respiratory syndrome ("SARS") or bird flu could disrupt our manufacturing operations, reduce demand for our customers' products and increase our supply chain costs. For example, our facility in Fuzhou, China, which manufactures custom optics components, was not permitted to resume operations after the Chinese Lunar New Year holiday until February 10, 2020, due to the spread of COVID-19 in China, which negatively affected our revenues for the three months ended March 27, 2020. In addition, we and some of our suppliers and customers in China experienced labor shortages during the three months ended March 27, 2020, due to travel restrictions imposed by the Chinese government. As COVID-19 has continued to spread throughout the world, authorities in other countries in which we have manufacturing facilities, including Thailand, the U.K. and the U.S., have implemented numerous measures to contain the virus, including travel bans and restrictions, quarantines, shelter-in-place orders, and business limitations and shutdowns. While we are unable to accurately predict the full impact that COVID-19 will have on our business, financial condition and operating results due to numerous uncertainties, including the duration and severity of the pandemic and containment measures, our compliance with these measures has impacted our day-to-day operations and could disrupt our business, as well as that of our customers, suppliers and other counterparties, for an indefinite period of time.

In addition, increased international political instability, evidenced by the threat or occurrence of terrorist attacks, enhanced national security measures, conflicts in the Middle East and Asia, strained international relations arising from these conflicts and the related decline in consumer confidence and economic weakness, may hinder our ability to do business. Any escalation in these events or similar future events may disrupt our operations and the operations of our customers and suppliers and may affect the availability of materials needed for our manufacturing services. Such events



may also disrupt the transportation of materials to our manufacturing facilities and finished products to our customers. These events have had, and may continue to have, an adverse impact on the U.S. and world economy in general, and customer confidence and spending in particular, which in turn could adversely affect our total revenues and operating results. The impact of these events on the volatility of the U.S. and world financial markets also could increase the volatility of the market price of our ordinary shares and may limit the capital resources available to us, our customers and our suppliers.

***We are not fully insured against all potential losses. Natural disasters or other catastrophes could adversely affect our business, financial condition and operating results.***

Our current property and casualty insurance covers loss or damage to our property and third-party property over which we have custody and control, as well as losses associated with business interruption, subject to specified exclusions and limitations such as coinsurance, facilities location sub-limits and other policy limitations and covenants. Even with insurance coverage, natural disasters or other catastrophic events, including acts of war, could cause us to suffer substantial losses in our operational capacity and could also lead to a loss of opportunity and to a potential adverse impact on our relationships with our existing customers resulting from our inability to produce products for them, for which we might not be compensated by existing insurance. This in turn could have a material adverse effect on our business, financial condition and operating results.

***Unfavorable worldwide economic conditions may negatively affect our business, financial condition and operating results.***

The sudden and continuing global economic downturn and uncertainty due to the effects of COVID-19 and subsequent volatility and adverse conditions in the capital and credit markets have negatively affected levels of business and consumer spending. Concerns about the increasing possibility of a global depression and potential default of various national bonds and debt backed by individual countries as well as the politics impacting these, could negatively impact the U.S. and global economies and adversely affect our financial results. In particular, the economic disruption caused by COVID-19 has led to reduced demand in some of our customers' optical communications product portfolios and significant volatility in global stock markets and currency exchange rates. Uncertainty about worldwide economic conditions poses a risk as businesses may further reduce or postpone spending in response to reduced budgets, tight credit, negative financial news and declines in income or asset values, which could adversely affect our business, financial condition and operating results and increase the volatility of our share price. In addition, our ability to access capital markets may be restricted, which could have an impact on our ability to react to changing economic and business conditions and could also adversely affect our business, financial condition and operating results.

***We may experience manufacturing yields that are lower than expected, potentially resulting in increased costs, which could harm our business, operating results and customer relations.***

Manufacturing yields depend on a number of factors, including the following:

- the quality of input, materials and equipment;
- the quality and feasibility of our customer's design;
- the repeatability and complexity of the manufacturing process;
- the experience and quality of training of our manufacturing and engineering teams; and
- the monitoring of the manufacturing environment.

Lower volume production due to continually changing designs generally results in lower yields. Manufacturing yields and margins can also be lower if we receive or inadvertently use defective or contaminated materials from our suppliers. In addition, our customer contracts typically provide that we will supply products at a fixed price each quarter, which assumes specific production yields and quality metrics. If we do not meet the yield assumptions and quality metrics used in calculating the price of a product, we may not be able to recover the costs associated with our failure to do so. Consequently, our operating results and profitability may be harmed.

***If the products that we manufacture contain defects, we could incur significant correction costs, demand for our services may decline and we may be exposed to product liability and product warranty claims, which could harm our business, financial condition, operating results and customer relations.***

We manufacture products to our customers' specifications, and our manufacturing processes and facilities must comply with applicable statutory and regulatory requirements. In addition, our customers' products and the manufacturing processes that we use to produce them are often complex. As a result, products that we manufacture may at times contain manufacturing or design defects, and our manufacturing processes may be subject to errors or fail to be in compliance with applicable statutory or regulatory requirements. Additionally, not all defects are immediately detectible. The testing procedures of our customers are generally limited to the evaluation of the products that we manufacture under likely and foreseeable failure scenarios. For various reasons (including, among others, the occurrence of performance problems that are unforeseeable at the time of testing or that are detected only when products are fully deployed and operated under peak stress conditions), these products may fail to perform as expected after their initial acceptance by a customer.

We generally provide a warranty of between one to five years on the products that we manufacture for our customers. This warranty typically guarantees that products will conform to our customers' specifications and be free from defects in workmanship. Defects in the products we manufacture, whether caused by a design, engineering, manufacturing or component failure or by deficiencies in our manufacturing processes and whether during or after the warranty period, could result in product or component failures, which may damage our business reputation, whether or not we are indemnified for such failures. We could also incur significant costs to repair or replace defective products under warranty, particularly when such failures occur in installed systems. In some instances, we may also be required to incur costs to repair or replace defective products outside of the warranty period in the event that a recurring defect is discovered in a certain percentage of a customer's products delivered over an agreed upon period of time. We have experienced product or component failures in the past and remain exposed to such failures, as the products that we manufacture are widely deployed throughout the world in multiple environments and applications. Further, due to the difficulty in determining whether a given defect resulted from our customer's design of the product or our manufacturing process, we may be exposed to product liability or product warranty claims arising from defects that are not our fault. In addition, if the number or type of defects exceeds certain percentage limitations contained in our contractual arrangements, we may be required to conduct extensive failure analysis, re-qualify for production or cease production of the specified products.

Product liability claims may include liability for personal injury or property damage. Product warranty claims may include liability to pay for a recall, repair or replacement of a product or component. Although liability for these claims is generally assigned to our customers in our contracts, even where they have assumed liability, our customers may not, or may not have the resources to, satisfy claims for costs or liabilities arising from a defective product. Additionally, under one of our contracts, in the event the products we manufacture do not meet the end-customer's testing requirements or otherwise fail, we may be required to pay penalties to our customer, including a fee during the time period that the customer or end-customer's production line is not operational as a result of the failure of the products that we manufacture, all of which could harm our business, operating results and customer relations. If we engineer or manufacture a product that is found to cause any personal injury or property damage or is otherwise found to be defective, we could incur significant costs to resolve the claim. While we maintain insurance for certain product liability claims, we do not maintain insurance for any recalls and, therefore, would be required to pay any associated costs that are determined to be our responsibility. A successful product liability or product warranty claim in excess of our insurance coverage or any material claim for which insurance coverage is denied, limited, is not available or has not been obtained could harm our business, financial condition and operating results.

***If we are unable to meet regulatory quality standards applicable to our manufacturing and quality processes for the products we manufacture, our business, financial condition or operating results could be harmed.***

As a manufacturer of products for the optics industry, we are required to meet certain certification standards, including the following: ISO9001 for Manufacturing Quality Management Systems; ISO14001 for Environmental Management Systems; TL9000 for Telecommunications Industry Quality Certification; IATF16949 for Automotive Industry Quality Certification; ISO13485 for Medical Devices Industry Quality Certification; AS9100 for Aerospace Industry Quality Certification; NADCAP (National Aerospace and Defense Contractors Accreditation Program) for Quality Assurance throughout the Aerospace and Defense Industries; and OHSAS18001 for Occupational Health and Safety Management Systems. We also maintain compliance with various additional standards imposed by the U.S. Food and Drug Administration ("FDA") with respect to the manufacture of medical devices.

Additionally, we are required to register with the FDA and other regulatory bodies and are subject to continual review and periodic inspection for compliance with various regulations, including testing, quality control and documentation procedures. We hold the following additional certifications: ANSI ESD S20.20 for facilities and manufacturing process

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control, in compliance with ESD standard; Transported Asset Protection Association, or TAPA, for Logistic Security Management System; and CSR-DIW for Corporate Social Responsibility in Thailand. In the European Union, we are required to maintain certain ISO certifications in order to sell our precision optical, electro-mechanical and electronic manufacturing services and we must undergo periodic inspections by regulatory bodies to obtain and maintain these certifications. If any regulatory inspection reveals that we are not in compliance with applicable standards, regulators may take action against us, including issuing a warning letter, imposing fines on us, requiring a recall of the products we manufactured for our customers, or closing our manufacturing facilities. If any of these actions were to occur, it could harm our reputation as well as our business, financial condition and operating results.

***If we fail to attract additional skilled employees or retain key personnel, our business, financial condition and operating results could suffer.***

Our future success depends, in part, upon our ability to attract additional skilled employees and retain our current key personnel. We have identified several areas where we intend to expand our hiring, including business development, finance, human resources, operations and supply chain management. We may not be able to hire and retain such personnel at compensation levels consistent with our existing compensation and salary structure. Our future also depends on the continued contributions of our executive management team and other key management and technical personnel, each of whom would be difficult to replace. Although we have key person life insurance policies on some of our executive officers, the loss of any of our executive officers or key personnel or the inability to continue to attract qualified personnel could harm our business, financial condition and operating results.

***Failure to comply with applicable environmental laws and regulations could have a material adverse effect on our business, financial condition and operating results.***

The sale and manufacturing of products in certain states and countries may subject us to environmental laws and regulations. In addition, rules adopted by the U.S. Securities and Exchange Commission (“SEC”) implementing the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010 impose diligence and disclosure requirements regarding the use of “conflict minerals” mined from the Democratic Republic of Congo and adjoining countries in the products we manufacture for our customers. Compliance with these rules has resulted in additional cost and expense, including for due diligence to determine and verify the sources of any conflict minerals used in the products we manufacture, and may result in additional costs of remediation and other changes to processes or sources of supply as a consequence of such verification activities. These rules may also affect the sourcing and availability of minerals used in the products we manufacture, as there may be only a limited number of suppliers offering “conflict free” metals that can be used in the products we manufacture for our customers.

Although we do not anticipate any material adverse effects based on the nature of our operations and these laws and regulations, we will need to ensure that we and, in some cases, our suppliers comply with applicable laws and regulations. If we fail to timely comply with such laws and regulations, our customers may cease doing business with us, which would have a material adverse effect on our business, financial condition and operating results. In addition, if we were found to be in violation of these laws, we could be subject to governmental fines, liability to our customers and damage to our reputation, which would also have a material adverse effect on our business, financial condition and operating results.

***We are subject to the risk of increased income taxes, which could harm our business, financial condition and operating results.***

We are subject to income and other taxes in Thailand, the PRC, the United Kingdom and the United States. Our effective income tax rate, provision for income taxes and future tax liability could be adversely affected by numerous factors, including the results of tax audits and examinations, income before taxes being lower than anticipated in countries with lower statutory tax rates and higher than anticipated in countries with higher statutory tax rates, changes in income tax rates, changes in the valuation of deferred tax assets and liabilities, failure to meet obligations with respect to tax exemptions, and changes in tax laws and regulations. As of March 27, 2020, our U.S. federal and state tax returns remain open to examination for the tax years 2014 through 2017. In addition, tax returns that remain open to examination in Thailand range from the tax years 2015 through 2019, and in the PRC and the United Kingdom range from the tax years 2015 through 2018. The results of audits and examinations of previously filed tax returns and continuing assessments of our tax exposures may have an adverse effect on our provision for income taxes and tax liability.

We base our tax position upon the anticipated nature and conduct of our business and upon our understanding of the tax laws of the various countries in which we have assets or conduct activities. However, our tax position is subject to review and possible challenge by tax authorities and to possible changes in law, which may have retroactive effect. Fabrinet (the “Cayman Islands Parent”) is an exempted company incorporated in the Cayman Islands. We maintain manufacturing operations in Thailand, the PRC, the United Kingdom and the U.S. We cannot determine in advance the extent to which some jurisdictions may require us to pay taxes or make payments in lieu of taxes. Under the current laws of the Cayman Islands, we are not subject to tax in the Cayman Islands on income or capital gains until March 6, 2039.

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Preferential tax treatment from the Thai government in the form of a corporate tax exemption is also currently available to us through June 2020 and June 2026 on income generated from projects to manufacture certain products at our Pinehurst campus and Chonburi campus, respectively. Such preferential tax treatment is contingent on various factors, including the export of our customers' products out of Thailand and our agreement not to move our manufacturing facilities out of our current province in Thailand for at least 15 years from the date on which preferential tax treatment was granted (i.e., at least until June 2020 in the case of our Pinehurst campus and until June 2026 in the case of our Chonburi campus). We will lose this favorable tax treatment in Thailand unless we comply with these restrictions, and as a result we may delay or forego certain strategic business decisions due to these tax considerations.

There is also a risk that Thailand or another jurisdiction in which we operate may treat the Cayman Islands Parent as having a permanent establishment in such jurisdiction and subject its income to tax. If we become subject to additional taxes in any jurisdiction or if any jurisdiction begins to treat the Cayman Islands Parent as having a permanent establishment, such tax treatment could materially and adversely affect our business, financial condition and operating results.

Certain of our subsidiaries provide products and services to, and may from time to time undertake certain significant transactions with, us and our other subsidiaries in different jurisdictions. For instance, we have intercompany agreements in place that provide for our California and Singapore subsidiaries to provide administrative services for the Cayman Islands Parent, and the Cayman Islands Parent has entered into manufacturing agreements with our Thai subsidiary. In general, related party transactions and, in particular, related party financing transactions, are subject to close review by tax authorities. Moreover, several jurisdictions in which we operate have tax laws with detailed transfer pricing rules that require all transactions with non-resident related parties to be priced using arm's length pricing principles and require the existence of contemporaneous documentation to support such pricing. Tax authorities in various jurisdictions could challenge the validity of our related party transfer pricing policies. Such a challenge generally involves a complex area of taxation and a significant degree of judgment by management. If any taxation authorities are successful in challenging our financing or transfer pricing policies, our income tax expense may be adversely affected and we could become subject to interest and penalty charges, which may harm our business, financial condition and operating results.

***We may not be able to obtain capital when desired on favorable terms, if at all, or without dilution to our shareholders.***

We anticipate that our current cash and cash equivalents, together with cash provided by operating activities and funds available through our working capital and credit facilities, will be sufficient to meet our current and anticipated needs for general corporate purposes for at least the next 12 months. We operate in a market, however, that makes our prospects difficult to evaluate. It is possible that we may not generate sufficient cash flow from operations or otherwise have the capital resources to meet our future capital needs. If this occurs, we may need additional financing to execute on our current or future business strategies.

Furthermore, if we raise additional funds through the issuance of equity or convertible debt securities, the percentage ownership of our shareholders could be significantly diluted, and these newly issued securities may have rights, preferences or privileges senior to those of existing shareholders. If adequate additional funds are not available or are not available on acceptable terms if and when needed, our ability to fund our operations, take advantage of unanticipated opportunities, develop or enhance our manufacturing services, hire additional technical and other personnel, or otherwise respond to competitive pressures could be significantly limited.

***The phase-out of the London Interbank Offered Rate ("LIBOR") could affect interest rates under our existing credit facility agreement, as well as our ability to seek future debt financing.***

LIBOR is the basic rate of interest used in lending between banks on the London interbank market and is widely used as a reference for setting the interest rates on loans globally. We generally use LIBOR as a reference rate to calculate interest rates under our credit facility agreement. In 2017, the United Kingdom's Financial Conduct Authority, which regulates LIBOR, announced that it intends to phase out LIBOR by the end of 2021. It is unclear if LIBOR will cease to exist at that time or if new methods of calculating LIBOR will be established such that it continues to exist after 2021. The U.S. Federal Reserve, in conjunction with the Alternative Reference Rates Committee, a steering committee comprised of large U.S. financial institutions, is considering replacing U.S. dollar LIBOR with a new index, the Secured Overnight Financing Rate ("SOFR"), calculated using short-term repurchase agreements backed by Treasury securities. Whether or not SOFR or another alternative reference rate attains market traction as a LIBOR replacement tool remains in question. If LIBOR ceases to exist, we will need to agree upon a replacement index with the bank under our credit facility agreement,

and certain of the interest rates under such agreement may change. The new rates may not be as favorable to us as those in effect prior to any LIBOR phase-out. In addition, the transition process may involve, among other things, increased volatility or illiquidity in markets for instruments that currently rely on LIBOR. The transition may also result in reductions in the value of certain instruments or the effectiveness of related transactions such as hedges, increased borrowing costs, uncertainty under applicable documentation, or difficult and costly consent processes. Any such effects of the transition away from LIBOR, as well as other unforeseen effects, may result in expenses, difficulties, complications or delays in connection with future financing efforts, which could have a material adverse impact on our business, financial condition and results of operations.

***Intellectual property infringement claims against our customers or us could harm our business, financial condition and operating results.***

Our services involve the creation and use of intellectual property rights, which subject us to the risk of intellectual property infringement claims from third parties and claims arising from the allocation of intellectual property rights among us and our customers.

Our customers may require that we indemnify them against the risk of intellectual property infringement arising out of our manufacturing processes. If any claims are brought against us or our customers for such infringement, whether or not these claims have merit, we could be required to expend significant resources in defense of such claims. In the event of an infringement claim, we may be required to spend a significant amount of time and money to develop non-infringing alternatives or obtain licenses. We may not be successful in developing such alternatives or obtaining such licenses on reasonable terms or at all, which could harm our business, financial condition and operating results.

***Any failure to protect our customers' intellectual property that we use in the products we manufacture for them could harm our customer relationships and subject us to liability.***

We focus on manufacturing complex optical products for our customers. These products often contain our customers' intellectual property, including trade secrets and know-how. Our success depends, in part, on our ability to protect our customers' intellectual property. We may maintain separate and secure areas for customer proprietary manufacturing processes and materials and dedicate floor space, equipment, engineers and supply chain management to protect our customers' proprietary drawings, materials and products. The steps we take to protect our customers' intellectual property may not adequately prevent its disclosure or misappropriation. If we fail to protect our customers' intellectual property, our customer relationships could be harmed and we may experience difficulty in establishing new customer relationships. In addition, our customers might pursue legal claims against us for any failure to protect their intellectual property, possibly resulting in harm to our reputation and our business, financial condition and operating results.

***We have incurred and will continue to incur significant increased costs as a result of operating as a public company, and our management will be required to continue to devote substantial time to various compliance initiatives.***

The Sarbanes-Oxley Act of 2002, the Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010, as well as other rules implemented by the SEC and the New York Stock Exchange ("NYSE"), impose various requirements on public companies, including requiring changes in corporate governance practices. These and proposed corporate governance laws and regulations under consideration may further increase our compliance costs. If compliance with these various legal and regulatory requirements diverts our management's attention from other business concerns, it could have a material adverse effect on our business, financial condition and operating results. The Sarbanes-Oxley Act requires, among other things, that we assess the effectiveness of our internal control over financial reporting annually and disclosure controls and procedures quarterly. While we were able to assert in our Annual Report on Form 10-K that our internal control over financial reporting was effective as of June 28, 2019, we cannot predict the outcome of our testing in future periods. If we are unable to assert in any future reporting periods that our internal control over financial reporting is effective (or if our independent registered public accounting firm is unable to express an opinion on the effectiveness of our internal controls), we could lose investor confidence in the accuracy and completeness of our financial reports, which would have an adverse effect on our share price.

Given the nature and complexity of our business and the fact that some members of our management team are located in Thailand while others are located in the U.S., control deficiencies may periodically occur. For example, following an internal investigation by the audit committee of our board of directors in September 2014 concerning various accounting cut-off issues, we identified certain significant deficiencies in our internal control over financial reporting, which have been remediated. While we have ongoing measures and procedures to prevent and remedy control deficiencies, if they occur there can be no assurance that we will be successful or that we will be able to prevent material weaknesses or significant deficiencies in our internal control over financial reporting in the future. Moreover, if we identify deficiencies in our internal control over financial reporting that are deemed to be material weaknesses in future periods, the market

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price of our ordinary shares could decline and we could be subject to potential delisting by the NYSE and review by the NYSE, the SEC, or other regulatory authorities, which would require the expenditure by us of additional financial and management resources. As a result, our shareholders could lose confidence in our financial reporting, which would harm our business and the market price of our ordinary shares.

***There are inherent uncertainties involved in estimates, judgments and assumptions used in the preparation of financial statements in accordance with U.S. GAAP. Any changes in estimates, judgments and assumptions could have a material adverse effect on our business, financial condition and operating results.***

The preparation of financial statements in accordance with U.S. GAAP involves making estimates, judgments and assumptions that affect reported amounts of assets (including intangible assets), liabilities and related reserves, revenues, expenses and income. Estimates, judgments and assumptions are inherently subject to change in the future, and any such changes could result in corresponding changes to the amounts of assets, liabilities, revenues, expenses and income. Any such changes could have a material adverse effect on our business, financial condition and operating results.

***The loan agreements for our long-term debt obligations and other credit facilities contain financial ratio covenants that may impair our ability to conduct our business.***

The loan agreements for our long-term and short-term debt obligations contain financial ratio covenants that may limit management's discretion with respect to certain business matters. These covenants require us to maintain a specified maximum total leverage ratio, minimum debt service coverage ratio (earnings before interest and depreciation and amortization plus cash on hand minus short-term debt), a minimum tangible net worth and a minimum quick ratio, which may restrict our ability to incur additional indebtedness and limit our ability to use our cash. In the event of our default on these loans or a breach of a covenant, the lenders may immediately cancel the loan agreement, deem the full amount of the outstanding indebtedness immediately due and payable, charge us interest on a monthly basis on the full amount of the outstanding indebtedness and, if we cannot repay all of our outstanding obligations, sell the assets pledged as collateral for the loan in order to fulfill our obligation. We may also be held responsible for any damages and related expenses incurred by the lender as a result of any default. Any failure by us or our subsidiaries to comply with these agreements could harm our business, financial condition and operating results.

***Our business could be negatively affected as a result of activist shareholders.***

If an activist investor takes an ownership position in our ordinary shares, responding to actions by such activist shareholder could be costly and time-consuming, disrupt our operations and divert the attention of management and our employees. Additionally, perceived uncertainties as to our future direction as a result of shareholder activism or changes to the composition of our board of directors may lead to the perception of a change in the direction of our business or other instability, which may be exploited by our competitors, cause concern to our current or potential customers, and make it more difficult to attract and retain qualified personnel. If customers choose to delay, defer or reduce transactions with us or do business with our competitors instead of us because of any such issues, then our business, financial condition and operating results would be adversely affected. In addition, our share price could experience periods of increased volatility as a result of shareholder activism.

***Our investment portfolio may become impaired by deterioration of the capital markets.***

We use professional investment management firms to manage our excess cash and cash equivalents. Our short-term investments as of March 27, 2020 are primarily investments in a fixed income portfolio, including certificates of deposit, time deposits, corporate bonds and commercial papers, U.S. agency and U.S. Treasury securities, and sovereign and municipal securities. Our investment portfolio may become impaired by deterioration of the capital markets. We follow an established investment policy and set of guidelines to monitor and help mitigate our exposure to interest rate and credit risk. The policy sets forth credit quality standards and limits our exposure to any one issuer, as well as our maximum exposure to various asset classes. The policy also provides that we may not invest in short-term investments with a maturity in excess of three years.

We regularly review our investment portfolio to determine if any security is other-than-temporarily impaired, which would require us to record an impairment charge in the period any such determination is made. In making this judgment, we evaluate, among other things, the duration and extent to which the fair value of a security is less than its cost; the financial condition of the issuer and any changes thereto; and our intent to sell, or whether we will more likely than not be required to sell, the security before recovery of its amortized cost basis. Our assessment on whether a security is other-than-temporarily impaired could change in the future due to new developments or changes in assumptions related to any particular security.



Should financial market conditions worsen, investments in some financial instruments may pose risks arising from market liquidity and credit concerns. In addition, any deterioration of the capital markets could cause our other income and expense to vary from expectations. As of March 27, 2020, we did not record any impairment charges associated with our portfolio of short-term investments, and although we believe our current investment portfolio has little risk of material impairment, we cannot predict future market conditions or market liquidity, or credit availability, and can provide no assurance that our investment portfolio will remain materially unimpaired.

***Energy price volatility may negatively impact our business, financial condition and operating results.***

We, along with our suppliers and customers, rely on various energy sources in our manufacturing and transportation activities. Energy prices have been subject to increases and volatility caused by market fluctuations, supply and demand, currency fluctuation, production and transportation disruption, world events and government regulations. While we are currently experiencing lower energy prices, a significant increase is possible, which could increase our raw material and transportation costs. In addition, increased transportation costs of our suppliers and customers could be passed along to us. We may not be able to increase our prices enough to offset these increased costs, and any increase in our prices may reduce our future customer orders, which could harm our business, financial condition and operating results.

**Risks Related to Ownership of Our Ordinary Shares**

***Our share price may be volatile due to fluctuations in our operating results and other factors, including the activities and operating results of our customers or competitors, any of which could cause our share price to decline.***

Our revenues, expenses and results of operations have fluctuated in the past and are likely to do so in the future from quarter-to-quarter and year-to-year due to the risk factors described in this section and elsewhere in this Quarterly Report on Form 10-Q. In addition to market and industry factors, the price and trading volume of our ordinary shares may fluctuate in response to a number of events and factors relating to us, our competitors, our customers and the markets we serve, many of which are beyond our control. Factors such as variations in our total revenues, earnings and cash flow, announcements of new investments or acquisitions, changes in our pricing practices or those of our competitors, commencement or outcome of litigation, sales of ordinary shares by us or our principal shareholders, fluctuations in market prices for our services and general market conditions could cause the market price of our ordinary shares to change substantially. Any of these factors may result in large and sudden changes in the volume and price at which our ordinary shares trade. Among other things, volatility and weakness in our share price could mean that investors may not be able to sell their shares at or above the prices they paid. Volatility and weakness could also impair our ability in the future to offer our ordinary shares or convertible securities as a source of additional capital and/or as consideration in the acquisition of other businesses.

Furthermore, the stock markets have experienced extreme price and volume fluctuations that have affected and continue to affect the market prices of equity securities of many companies. These fluctuations often have been unrelated or disproportionate to the operating performance of those companies. These broad market and industry fluctuations, as well as general economic, political and market conditions such as recessions, interest rate changes or international currency fluctuations, may cause the market price of our ordinary shares to decline. In the past, companies that have experienced volatility in the market price of their stock have been subject to securities class action litigation. We may be the target of this type of litigation in the future. Securities litigation against us could result in substantial costs and divert our management's attention from other business concerns, which could seriously harm our business.

***If securities or industry analysts do not publish research or if they publish misleading or unfavorable research about our business, the market price and trading volume of our ordinary shares could decline.***

The trading market for our ordinary shares depends in part on the research and reports that securities or industry analysts publish about us or our business. If securities or industry analysts stop covering us, or if too few analysts cover us, the market price of our ordinary shares could be adversely impacted. If one or more of the analysts who covers us downgrades our ordinary shares or publishes misleading or unfavorable research about our business, our market price would likely decline. If one or more of these analysts ceases coverage of us or fails to publish reports on us regularly, demand for our ordinary shares could decrease, which could cause the market price or trading volume of our ordinary shares to decline.

***We may become a passive foreign investment company, which could result in adverse U.S. tax consequences to U.S. investors.***

Based upon estimates of the value of our assets, which are based in part on the trading price of our ordinary shares, we do not expect to be a passive foreign investment company (“PFIC”) for U.S. federal income tax purposes for the taxable year 2020 or for the foreseeable future. However, despite our expectations, we cannot assure you that we will not be a PFIC for the taxable year 2020 or any future year because our PFIC status is determined at the end of each year and depends on the composition of our income and assets during such year. If we are a PFIC, our U.S. investors will be subject to increased tax liabilities under U.S. tax laws and regulations and to burdensome reporting requirements.

***Certain provisions in our constitutional documents may discourage our acquisition by a third party, which could limit your opportunity to sell shares at a premium.***

Our constitutional documents include provisions that could limit the ability of others to acquire control of us, modify our structure or cause us to engage in change-of-control transactions, including, among other things, provisions that:

- establish a classified board of directors;
- prohibit our shareholders from calling meetings or acting by written consent in lieu of a meeting;
- limit the ability of our shareholders to propose actions at duly convened meetings; and
- authorize our board of directors, without action by our shareholders, to issue preferred shares and additional ordinary shares.

These provisions could have the effect of depriving you of an opportunity to sell your ordinary shares at a premium over prevailing market prices by discouraging third parties from seeking to acquire control of us in a tender offer or similar transaction.

***Our shareholders may face difficulties in protecting their interests because we are incorporated under Cayman Islands law.***

Our corporate affairs are governed by our amended and restated memorandum and articles of association (“MOA”), by the Companies Law (as amended) of the Cayman Islands and the common law of the Cayman Islands. The rights of our shareholders and the fiduciary responsibilities of our directors under the laws of the Cayman Islands are not as clearly established under statutes or judicial precedent as in jurisdictions in the U.S. Therefore, you may have more difficulty in protecting your interests than would shareholders of a corporation incorporated in a jurisdiction in the U.S., due to the comparatively less developed nature of Cayman Islands law in this area.

The Companies Law permits mergers and consolidations between Cayman Islands companies and between Cayman Islands companies and non-Cayman Islands companies. Dissenting shareholders have the right to be paid the fair value of their shares (which, if not agreed between the parties, will be determined by the Cayman Islands court) if they follow the required procedures, subject to certain exceptions. Court approval is not required for a merger or consolidation which is effected in compliance with these statutory procedures.

In addition, there are statutory provisions that facilitate the reconstruction and amalgamation of companies, provided that the arrangement is approved by a majority in number of each class of shareholders and creditors with whom the arrangement is to be made, and who must in addition represent three-fourths in value of each such class of shareholders or creditors, as the case may be, that are present and voting either in person or by proxy at a meeting convened for that purpose. The convening of the meeting and subsequently the arrangement must be sanctioned by the Grand Court of the Cayman Islands. A dissenting shareholder has the right to express to the court the view that the transaction ought not to be approved.

When a takeover offer is made and accepted by holders of 90.0% of the shares within four months, the offeror may, within a two-month period, require the holders of the remaining shares to transfer such shares on the terms of the offer. An objection can be made to the Grand Court of the Cayman Islands but is unlikely to succeed unless there is evidence of fraud, bad faith or collusion.

If the arrangement and reconstruction is thus approved, the dissenting shareholder would have no rights comparable to appraisal rights, which would otherwise ordinarily be available to dissenting shareholders of a corporation incorporated in a jurisdiction in the U.S., providing rights to receive payment in cash for the judicially determined value of the shares. This may make it more difficult for you to assess the value of any consideration you may receive in a merger or consolidation or to require that the offeror give you additional consideration if you believe the consideration offered is insufficient.



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Shareholders of Cayman Islands exempted companies have no general rights under Cayman Islands law to inspect corporate records and accounts or to obtain copies of lists of shareholders. Our directors have discretion under our MOA to determine whether or not, and under what conditions, our corporate records may be inspected by our shareholders, but are not obliged to make them available to our shareholders. This may make it more difficult for you to obtain the information needed to establish any facts necessary for a shareholder motion or to solicit proxies from other shareholders in connection with a proxy contest.

Subject to limited exceptions, under Cayman Islands law, a minority shareholder may not bring a derivative action against the board of directors.

### ***Certain judgments obtained against us by our shareholders may not be enforceable.***

The Cayman Islands Parent is a Cayman Islands exempted company and substantially all of our assets are located outside of the U.S. Given our domicile and the location of our assets, it may be difficult to enforce in U.S. courts judgments obtained against us in U.S. courts based on the civil liability provisions of the U.S. federal securities laws. In addition, there is uncertainty as to whether the courts of the Cayman Islands, Thailand or the PRC would recognize or enforce judgments of U.S. courts against us predicated upon the civil liability provisions of the securities laws of the U.S. or any state. In particular, a judgment in a U.S. court would not be recognized and accepted by Thai courts without a re-trial or examination of the merits of the case. In addition, there is uncertainty as to whether such Cayman Islands, Thai or PRC courts would be competent to hear original actions brought in the Cayman Islands, Thailand or the PRC against us predicated upon the securities laws of the U.S. or any state.

## **ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS**

### ***Sales of Unregistered Securities***

Not applicable.

### ***Purchases of Equity Securities by the Issuer and Affiliated Purchasers***

On August 21, 2017, we announced that our board of directors had approved a share repurchase program to permit us to repurchase up to \$30.0 million worth of our issued and outstanding ordinary shares in the open market in accordance with applicable rules and regulations, at such time and such prices as management may decide. In February 2018 and May 2019, we announced that our board of directors approved increases of \$30.0 million and \$50.0 million, respectively, to the original share repurchase authorization, bringing the aggregate authorization to \$110.0 million. The repurchased shares will be held as treasury stock. During the three months ended March 27, 2020, we repurchased 355,000 shares under the program at an average price per share of \$58.37, totaling \$20.7 million. As of March 27, 2020, we had a remaining authorization to purchase up to \$41.5 million worth of our ordinary shares.

The following table summarizes share repurchase activity for the three months ended March 27, 2020:

<u>Period</u>	<u>Total Number of Shares Purchased</u>	<u>Average Price Paid Per Share</u>	<u>Total Number of Shares Purchased As Part of Publicly Announced Program</u>	<u>Maximum Approximate Dollar Value of Shares That May Yet Be Purchased Under the Program</u>
December 28, 2019 – January 24, 2020	—	\$ —	—	\$ 62,220,607
January 25, 2020 – February 21, 2020	—	\$ —	—	\$ 62,220,607
February 22, 2020 – March 27, 2020	355,000	\$ 58.37	355,000	\$ 41,499,413
Total	<u>355,000</u>	<u>\$ 58.37</u>	<u>355,000</u>	<u>\$ 41,499,413</u>

**ITEMS 3, 4 and 5 are not applicable and have been omitted.**

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### ITEM 6. EXHIBITS

<u>Exhibit Number</u>	<u>Description</u>	<u>Incorporated by reference herein</u>		
		<u>Form</u>	<u>Exhibit No.</u>	<u>Filing Date</u>
10.1	<a href="#">Amended and restated offer letter, dated February 1, 2020, between Toh-Seng Ng and Fabrinet USA, Inc.</a>	8-K	10.1	February 3, 2020
10.2	<a href="#">Amended and restated offer letter, dated March 17, 2020, between Csaba Sverha and Fabrinet USA, Inc.</a>			
31.1	<a href="#">Certification of Chief Executive Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</a>			
31.2	<a href="#">Certification of Chief Financial Officer pursuant to Exchange Act Rules 13a-14(a) and 15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002</a>			
32.1*	<a href="#">Certifications of Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002</a>			
101.INS	Inline XBRL Instance.			
101.SCH	Inline XBRL Taxonomy Extension Schema.			
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase.			
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase.			
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase.			
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase.			
104	Cover Page Interactive Data File (formatted as inline XBRL and contained in Exhibit 101).			

\* The certifications attached as Exhibit 32.1 that accompany this Quarterly Report on Form 10-Q, are deemed furnished and not filed with the Securities and Exchange Commission and are not to be incorporated by reference into any filing of Fabrinet under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, whether made before or after the date of this Quarterly Report on Form 10-Q, irrespective of any general incorporation language contained in such filing.

**SIGNATURE**

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

**FABRINET**

Date: May 5, 2020

/s/ CSABA SVERHA

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Csaba Sverha  
Executive Vice President, Chief Financial Officer  
(Principal Financial and Accounting Officer)



Fabrinet USA Inc.  
4900 Patrick Henry Drive  
Santa Clara, CA 95054

March 17, 2020

Csaba Sverha

c/o Fabrinet USA, Inc.  
4900 Patrick Henry Drive  
Santa Clara, California 95054

Dear Csaba,

This letter is intended to amend and restate your offer letter dated March 9, 2018, which extended to you an offer of employment, and which you accepted on March 14, 2018, for the position Vice President—Operations Finance of Fabrinet USA, Inc. (“FUSA” or the “Company”), a wholly owned subsidiary of Fabrinet. This letter will formalize the updated terms of your employment by the Company given your promotion to Executive Vice President and the Chief Financial Officer (“CFO”) of Fabrinet effective February 17, 2020.

While employed by FUSA as CFO of Fabrinet, you will report to Mr. Seamus Grady, its Chief Executive Officer. Your duties and responsibilities will generally consist of those associated with managing all financial, taxes, treasury and investor relations of Fabrinet. You will devote substantially all of your business time and efforts to the performance of those duties and use your best efforts in doing so.

While employed by the Company, you will be required at times to travel to and work in the various company locations, including Thailand, the Cayman Islands, the U.S., the U.K., and Israel, as well other non-company locations.

Acceptance of this offer constitutes your representation that your execution of this agreement and performance of the requirements of this position will not be in violation of any other agreement to which you are a party.

#### *Compensation & Benefits*

While employed by the Company as CFO, your compensation and benefits will include:

**Base Salary.** Your annual base salary will be US \$450,000.00, which will be paid on a semi-monthly basis on or about the 15th and last day of each month in accordance with FUSA’s payroll policy, subject to applicable U.S. tax withholdings. Your base salary will be subject to review and adjustment by the Compensation Committee of the Board of Directors of Fabrinet from time to time in its sole discretion.

**Bonus.** Subject to the Board’s approval, you will be eligible to participate in Fabrinet’s 2020 Executive Incentive Plan, including the award of an annual target bonus. Any such target bonus, or portion thereof, will be paid as soon as practicable after the Compensation Committee of the Board of Directors determines that the target bonus (or relevant portion thereof) has been earned, but in no event shall any such target bonus be paid later than sixty (60) days following the applicable target bonus performance period. Receipt of any target bonus is contingent upon your continued employment with FUSA through the date the bonus is paid. The target bonus initially will be set at up to sixty percent (60%) of your base annual salary, pro-rated for the balance of Fabrinet’s current fiscal year, which may be adjusted from time to time going forward by the Compensation Committee of Fabrinet’s Board of Directors.

**Benefits.** You will be eligible to participate in FUSA’s Employee Benefits Plan, which includes (a) one-hundred twenty (120) hours paid time off (PTO) per year, (b) company paid healthcare insurance (medical, dental & vision for you and your eligible dependents), (c) a 401(k) plan with a company paid match capped at 6% of your base salary per month up to US \$15,000 per year, and (d) Group Term Life insurance, subject to the particulars of the plan.

**Restricted Stock Units.** You will be awarded time based Restricted Stock Units (“RSUs”) valued in the amount of US \$124,658 covering ordinary shares of Fabrinet, in accordance with the terms of Fabrinet’s 2020 Equity Incentive Plan (the “Plan”) and Fabrinet’s standard form of restricted stock unit agreement under the Plan. The actual number of RSUs awarded will be equal to such value, divided by the closing market price of a share on the third trading day following the day on which the Fabrinet earnings release occurs for Fabrinet’s fiscal quarter in which the RSUs for all participants in the Plan are approved by the Committee, with any resulting fractional number of shares rounded down to the nearest whole number of shares. This award is subject to your continued employment with FUSA through the award’s grant date. This RSU award will vest over a period of three (3) year as follows: 33% of the RSU award will vest on the anniversary of the Vesting Commencement Date in each of the following three (3) years, provided you are employed by FUSA continuously to and through each such date.

You also will be awarded performance based RSUs valued in the amount of US \$249,316, half of which will be normal performance RSUs and half which will be stretch awards, which will vest, if at all, on the date the Compensation Committee certifies the achievement of the cumulative performance criteria set by the Board for Fabrinet’s fiscal years 2020 and 2021.

**Ex Patriate Benefits.** You will also receive the following benefits each month during the time you are required to work and reside in Thailand:

- You will receive a Cost of Living Allowance (“COLA”) or expatriate living allowance of US \$10,000.00 per month, paid on a semi-monthly basis on or about the 15<sup>th</sup> and 30<sup>th</sup> of each month during the time you are required to work and reside in Thailand. This COLA payment will be tax equalized and added to your regular payroll deposits.
- A car and driver will be provided to you for business-related local transportation purposes in Thailand.
- You will be enrolled in the Expatriate US tax equalization program offered by FUSA, which includes full tax equalization for US and California income taxes, and the services of Ernst & Young (our expatriate tax consultants).
- An annual, tax equalized travel allowance of \$15,000 for you, your wife and your two children.
- The Company will reimburse the reasonable annual school fees and advance payments you may incur in connection with your children’s attendance at an international school in Thailand, including deposits, surety bonds, and the like, which reimbursements will be tax equalized.
- If and upon termination of your employment while you are assigned to a location outside of the U.S., you will be repatriated back to the US, which will include one-way ticket economy airfare and, as pre-approved, reasonable moving expenses for the shipment of your personal items back to your US home address (the “Repatriation Benefits”). Also, tax equalization services will be provided for the tax year that your employment ended with FUSA, in accordance with the terms of FUSA’s US Expatriate tax equalization program. The expenses covered by the Repatriation Benefits must be incurred no later than the last day of the second calendar year following the calendar year in which you have a separation from service from FUSA, within the meaning of Section 409A (as defined below). Reimbursements related to the Repatriation Benefits, if any, will be paid no later than the third calendar year following the calendar year in which you have a separation from service from FUSA.
- Upon the termination of your employment with FUSA, the Repatriation Benefits are intended to be, are exclusive and in lieu of, and supersede any other rights or remedies to which you otherwise may be entitled, whether at law, tort or contract or in equity, or under this letter (other than the payment of accrued but unpaid wages, as required by law, and any unreimbursed reimbursable expenses). You will not be entitled to any benefits, compensation or other payments or rights upon a termination of your employment with FUSA, other than the Repatriation Benefits as set forth in this letter.

**Business Expenses.** The Company will reimburse you for reasonable travel or other expenses incurred by you in the furtherance of or in connection with the performance of your duties under this Letter, in accordance with the Company's expense reimbursement policy as may be in effect from time to time.

This offer is not to be considered a contract guaranteeing employment for any specific duration. Employment with FUSA is on an at-will basis. You are thus free to terminate your employment with FUSA for any reason at any time with or without prior notice. Similarly, FUSA may terminate the employment relationship with or without cause or notice

*Section 409A US Treasury Regulation*

Each payment and benefit payable under this letter is intended to constitute a separate payment for purposes of Section 1.409A-2(b) (2) of the Treasury Regulations. The foregoing provisions are intended to comply with the requirements of Section 409A of the Internal Revenue Code of 1986, as amended, and the final regulations and official guidance thereunder ("Section 409A") such that none of the payments and benefits provided hereunder will be subject to the additional tax imposed under Section 409A, and any ambiguities herein will be interpreted to so comply

Notwithstanding anything to the contrary in this letter, no severance payments or benefits to be paid or provided to you, if any, under this letter that, when considered together with any other severance payments or separation benefits, are considered deferred compensation under Section 409A (together, the "Deferred Payments") will be paid or provided until you have a "separation from service" within the meaning of Section 409A. Similarly, no severance payable to you, if any, under this letter that otherwise would be exempt from Section 409A pursuant to Treasury Regulation Section 1.409A-1(b)(9) will be payable until you have a "separation from service" within the meaning of Section 409A. In no event will you have the discretion to determine the taxable year of payment of any Deferred Payment.

You agree we will work together in good faith to consider amendments to this letter, if required, and to take such reasonable actions, as necessary, appropriate or desirable to avoid imposition of any additional tax or income recognition prior to actual payment to you under Section 409A. In no event will the Company reimburse you for any taxes that may be imposed on you as result of Section 409A.

Notwithstanding anything to the contrary in this letter, if you are a "specified employee" within the meaning of Section 409A at the time of your separation from service (other than due to death), then the Deferred Payments, if any, that are payable within the first six (6) months following your separation from service, will become payable on the date six (6) months and one (1) day following the date of your separation from service. All subsequent Deferred Payments, if any, will be payable in accordance with the payment schedule applicable to each payment or benefit. Notwithstanding anything herein to the contrary, in the event of your death following your separation from service, but before the six (6) month anniversary of the separation from service, any payments delayed in accordance with this paragraph will be payable in a lump sum as soon as administratively practicable after the date of your death and all other Deferred Payments will be payable in accordance with the payment schedule applicable to each payment or benefit.

During the term of your employment, and for a one-year period immediately following the termination of your employment, you shall not, without FUSA's prior written consent:

- (i) solicit or encourage to leave the employment or other service of FUSA, Fabrinet (Cayman) or the affiliates of either, any employee or independent contractor thereof, or hire (on behalf of yourself or any other person or entity) any employee or independent contractor who has left the employment or other service of FUSA, Fabrinet (Cayman) or the affiliates of either within the one-year period that follows the termination of such employee's or independent contractor's employment or other service with FUSA, Fabrinet (Cayman) or the affiliates of either; or

(ii) whether for your own account or for the account of any other person, firm, corporation or other business organization, intentionally interfere with FUSA's, Fabrinet (Cayman)'s or any of their affiliates' relationship with, or endeavor to entice away from FUSA, Fabrinet (Cayman) or the affiliates of either, any person who during the term of your employment or the one-year period following the expiration of the term of your employment is or was a customer or client of FUSA, Fabrinet (Cayman) or the affiliates of either.

Also, please be advised it is the policy of FUSA to maintain a workplace that is free of drugs and alcohol, and that any violation of this policy will constitute grounds for the immediate termination of your employment.

Should you have questions or require additional information about any benefits, terms or conditions of your employment, please do not hesitate to Edward T. Attanasio, Senior Vice President, Worldwide Human Resources, by telephone at \_\_\_\_\_ or email at \_\_\_\_\_.

If you are in agreement with and accept the terms of this offer of employment, please indicate your acceptance by signing this letter in the space provided below, noting also your employment start date, and by returning a copy of the signed letter to me at your earliest convenience.

Sincerely,

/s/ Seamus Grady

\_\_\_\_\_  
Seamus Grady  
Chief Executive Officer  
Fabrinet

\*\*\* \*\*

I accept this amended offer of employment with FUSA under the terms set forth in this letter. I acknowledge this letter is the complete agreement concerning my employment and supersedes all prior or concurrent agreements and representations and may not be modified in any way except in a writing executed by an authorized agent of FUSA.

/s/ Csaba Sverha

\_\_\_\_\_  
Csaba Sverha

April 14, 2020

Date

## CERTIFICATION

I, Seamus Grady, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Fabrinet;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 5, 2020

/s/ SEAMUS GRADY

Seamus Grady

Chief Executive Officer (Principal Executive Officer)



## CERTIFICATION

I, Csaba Sverha, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Fabrinet;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 5, 2020

/s/ CSABA SVERHA

Csaba Sverha  
Executive Vice President, Chief Financial Officer (Principal  
Financial and Accounting Officer)

## CERTIFICATIONS OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER

**PURSUANT TO  
18 U.S.C. SECTION 1350,  
AS ADOPTED PURSUANT TO  
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

I, Seamus Grady, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q of Fabrinet for the fiscal quarter ended March 27, 2020 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in this Quarterly Report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Fabrinet.

Date: May 5, 2020

By: /s/ SEAMUS GRADY

Name: Seamus Grady

Title: Chief Executive Officer (Principal Executive Officer)

I, Csaba Sverha, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report on Form 10-Q of Fabrinet for the fiscal quarter ended March 27, 2020 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in this Quarterly Report on Form 10-Q fairly presents, in all material respects, the financial condition and results of operations of Fabrinet.

Date: May 5, 2020

By: /s/ CSABA SVERHA

Name: Csaba Sverha

Title: Executive Vice President, Chief Financial Officer  
(Principal Financial and Accounting Officer)