WESCO INTERNATIONAL INC
Form 10-Q
May 06, 2009

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended March 31, 2009

Or

o **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 001-14989

WESCO International, Inc.

(Exact name of registrant as specified in its charter)

Delaware	**25-1723342**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)
225 West Station Square Drive Suite 700 Pittsburgh, Pennsylvania 15219	**(412) 454-2200**
(Address of principal executive offices)	(Registrant s telephone number, including area code)

N/A

(Former name or former address, if changed since last report)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or such shorter period that the registrant was required to submit and post such files). Yes o No o

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

Large accelerated filer þ	Accelerated filer o	Non-accelerated filer o	Smaller reporting company o

(Do not check if a smaller reporting company)

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

As of May 4, 2009, WESCO International, Inc. had 42,259,962 shares of common stock outstanding.

WESCO INTERNATIONAL, INC. AND SUBSIDIARIES
QUARTERLY REPORT ON FORM 10-Q
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WESCO INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(unaudited)

Amounts in thousands, except share data	**March 31, 2009**	**December 31, 2008 [1]**
Assets		
Current Assets:		
Cash and cash equivalents	$ 105,135	$ 86,338
Trade accounts receivable, net of allowance for doubtful accounts of $18,373 and $19,665 in 2009 and 2008, respectively	687,801	791,356
Other accounts receivable	45,427	42,758
Inventories, net	561,070	605,678
Current deferred income taxes	2,856	2,857
Income taxes receivable	20,751	18,661
Prepaid expenses and other current assets	9,896	10,015
Total current assets	1,432,936	1,557,663
Property, buildings and equipment, net	116,859	119,223
Intangible assets, net	86,774	88,689
Goodwill	863,010	862,778
Investment in subsidiary	45,684	46,251
Deferred income taxes	15,892	16,811
Other assets	11,547	28,446
Total assets	$ 2,572,702	$ 2,719,861
Liabilities and Stockholders Equity		
Current Liabilities:		
Accounts payable	$ 524,261	$ 571,832
Accrued payroll and benefit costs	33,612	49,753
Short-term debt	245,000	295,000
Current portion of long-term debt	3,847	3,823
Bank overdrafts	18,419	30,367
Current deferred income taxes	1,467	1,516
Other current liabilities	50,271	53,718
Total current liabilities	876,877	1,006,009
Long-term debt, net of discount of $36,655 and $40,501 in 2009 and 2008, respectively	757,201	801,427
Deferred income taxes	139,630	136,736
Other noncurrent liabilities	23,299	20,585
Total liabilities	$ 1,797,007	$ 1,964,757

Commitments and contingencies		
Stockholders Equity:		
Preferred stock, $.01 par value; 20,000,000 shares authorized, no shares issued or outstanding		
Common stock, $.01 par value; 210,000,000 shares authorized, 55,803,620 and 55,788,620 shares issued and 42,254,962 and 42,239,962 shares outstanding in 2009 and 2008, respectively	558	557
Class B nonvoting convertible common stock, $.01 par value; 20,000,000 shares authorized, 4,339,431 issued and no shares outstanding in 2009 and 2008, respectively	43	43
Additional capital	889,353	886,019
Retained earnings	500,373	477,111
Treasury stock, at cost; 17,888,089 shares in 2009 and 2008	(590,288)	(590,288)
Accumulated other comprehensive income	(24,344)	(18,338)
Total stockholders equity	775,695	755,104
Total liabilities and stockholders equity	$ 2,572,702	$ 2,719,861

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

(1) The balances reported as of December 31, 2008 have been revised as a result of the retrospective application of FSP ABP 14-1 on January 1, 2009 (see Note 3 Accounting for Convertible Debt Instruments).

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WESCO INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(unaudited)

Amounts in thousands, except per share data	**Three Months Ended March 31, 2009**	**Three Months Ended March 31, 2008 (1)**
Net sales	$1,179,590	$1,465,206
Cost of goods sold (excluding depreciation and amortization below)	941,413	1,169,561
Selling, general and administrative expenses	187,489	211,639
Depreciation and amortization	7,157	6,933
Income from operations	43,531	77,073
Interest expense, net	12,518	18,082
Other income	(1,626)	(2,744)
Income before income taxes	32,639	61,735
Provision for income taxes	9,377	19,045
Net income	$ 23,262	$ 42,690
Earnings per share :		
Basic	$ 0.55	$ 1.00
Diluted	$ 0.55	$ 0.97

(1) The balances reported for the three months ended March 31, 2008 have been revised as a result of the retrospective application of FSP ABP 14-1 on January 1, 2009 (see Note 3 Accounting for Convertible Debt Instruments).

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

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WESCO INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

	Three Months Ended March, 31	
Amounts in thousands	**2009**	**2008** [1]
Operating Activities:		
Net income	$ 23,262	$ 42,690
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	7,157	6,933
Amortization of debt issuance costs	858	839
Amortization of debt discount	3,846	3,628
Deferred income taxes	2,537	(1,379)
Stock-based compensation expense	3,161	3,223
Loss on sale of property, buildings and equipment	201	
Loss on sale of subsidiary		3,005
Equity income, net of distributions in 2009 of $2,237	611	(2,744)
Excess tax benefit from stock-based compensation	(62)	(1,568)
Interest related to uncertain tax positions	222	232
Changes in assets and liabilities		
Trade and other receivables, net	113,854	(16,896)
Inventories, net	42,880	26,904
Prepaid expenses and other current assets	(1,466)	8,211
Accounts payable	(45,395)	23,418
Accrued payroll and benefit costs	(16,062)	(14,468)
Other current and noncurrent liabilities	(1,010)	9,933
Net cash provided by operating activities	134,594	91,961
Investing Activities:		
Capital expenditures	(2,856)	(11,319)
Acquisition payments	(74)	(96)
Proceeds from sale of subsidiary		60,000
Proceeds from sale of assets	82	13
Net cash (used) provided by investing activities	(2,848)	48,598
Financing Activities:		
Short-term (repayments) borrowings, net	(50,000)	3,000
Proceeds from issuance of long-term debt	71,000	241,500
Repayments of long-term debt	(118,871)	(324,133)
Proceeds from the exercise of stock options	112	2,233
Excess tax benefit from stock-based compensation	62	1,568
Repurchase of common stock		(24,933)
Decrease in bank overdrafts	(11,948)	(14,862)
Payments on capital lease obligations	(683)	(499)

Net cash used by financing activities	(110,328)	(116,126)
Effect of exchange rate changes on cash and cash equivalents	(2,621)	(2,298)
Net change in cash and cash equivalents	18,797	22,135
Cash and cash equivalents at the beginning of period	86,338	72,297
Cash and cash equivalents at the end of period	$ 105,135	$ 94,432
Supplemental disclosures:		
Non-cash investing and financing activities:		
Property, buildings and equipment acquired through capital leases	507	574

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

(1) The balances reported for the three months ended March 31, 2008 have been revised as a result of the retrospective application of FSP ABP 14-1 on January 1, 2009.
(see Note 3 Accounting for Convertible Debt Instruments).

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WESCO INTERNATIONAL, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. ORGANIZATION

WESCO International, Inc. and its subsidiaries (collectively, WESCO or the Company), headquartered in Pittsburgh, Pennsylvania, is a full-line distributor of electrical supplies and equipment and is a provider of integrated supply procurement services with operations in the United States, Canada, Mexico, the United Kingdom, Nigeria, United Arab Emirates, Singapore, Australia and China. WESCO currently operates approximately 400 full service branch locations and seven distribution centers (four in the United States and three in Canada.)

2. ACCOUNTING POLICIES

Basis of Presentation

The unaudited condensed consolidated financial statements of WESCO have been prepared in accordance with Rule 10-01 of Regulation S-X of the Securities and Exchange Commission (the SEC). The unaudited condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in WESCO s 2008 Annual Report on Form 10-K filed with the SEC. The December 31, 2008 condensed consolidated balance sheet data was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States.

The unaudited condensed consolidated balance sheet as of March 31, 2009, the unaudited condensed consolidated statements of income for the three months ended March 31, 2009 and 2008, respectively, and the unaudited condensed consolidated statements of cash flows for the three months ended March 31, 2009 and 2008, respectively, in the opinion of management, have been prepared on the same basis as the audited consolidated financial statements and include all adjustments necessary for the fair statement of the results of the interim periods. All adjustments reflected in the unaudited condensed consolidated financial statements are of a normal recurring nature unless indicated. Results for the interim periods presented are not necessarily indicative of the results to be expected for the full year.

Recent Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board (the FASB) issued Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements* (SFAS 157) which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This statement applies whenever other accounting standards require or permit assets or liabilities to be measured at fair value but does not expand the use of fair value to new accounting transactions and does not apply to pronouncements that address share-based payment transactions. On February 12, 2008, the FASB issued FASB Staff Position (FSP) SFAS No. 157-2, Effective Date of SFAS No. 157. The FSP amends SFAS 157 to delay the effective date of SFAS 157 for all nonfinancial assets and liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (that is, at least annually) to fiscal years beginning after November 15, 2008. Except for the delay for nonfinancial assets and liabilities, SFAS 157 was effective for fiscal years beginning after November 15, 2007. Consistent with its requirements, WESCO adopted SFAS 157 for its financial assets and liabilities on January 1, 2008. WESCO s financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable, bank overdrafts and debt. The Company believes that the recorded values of its financial instruments, except for long-term debt, approximate fair value because of their nature and respective duration. The partial adoption of SFAS 157 did not impact WESCO s financial position, results of operations, or cash flows. On January 1, 2009, WESCO adopted SFAS 157 for its nonfinancial assets and liabilities which include those measured at fair value in goodwill and indefinite lived intangible asset impairment testing, and assets acquired and liabilities assumed in a business combination. The adoption of SFAS 157 for nonfinancial assets and liabilities did not impact WESCO s financial position, results of operations or cash flows. However, in the event that WESCO acquires a new business or has an impairment issue related to goodwill or indefinite lived intangible assets, the determination of fair value of the assets and liabilities will be subject to SFAS 157.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), *Business Combinations* (SFAS 141R) which establishes additional principles and requirements for how the acquirer in a business combination recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed and any noncontrolling interest in the acquiree at the acquisition date fair value. SFAS 141R is designed to improve the relevance, representational faithfulness, and comparability of the financial information that a reporting entity provides in its financial reports about a business combination and its effects. SFAS 141R applies prospectively to business combinations for which the acquisition date is in or after the beginning of the first annual reporting period beginning after December 15, 2008. As there were no acquisitions executed in the first quarter of 2009, the adoption of SFAS 141R did not impact WESCO s financial position, results of operations or cash flows.

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In April 2008, the FASB issued FSP No. FAS 142-3, *Determination of the Useful Life of Intangible Assets* (FSP FAS 142-3) which amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under SFAS No. 142, *Goodwill and Other Intangible Assets* (SFAS 142), and requires additional disclosure. The objective of FSP FAS 142-3 is to improve the consistency between the useful life of a recognized intangible asset under SFAS 142 and the period of expected cash flows used to measure the fair value of the asset under SFAS 141R and other generally accepted accounting principles. FSP FAS 142-3 is effective for fiscal years beginning after December 15, 2008 and shall be applied prospectively to intangible assets acquired after the effective date. The adoption of FSP FAS 142-3 did not impact WESCO s financial position, results of operations or cash flows.

3. ACCOUNTING FOR CONVERTIBLE DEBT INSTRUMENTS

On January 1, 2009, WESCO retrospectively applied the provisions of FSP APB 14-1, *Accounting for Convertible Debt Instruments That May Be Settled in Cash Upon Conversion (Including Partial Cash Settlement)* (FSP APB 14-1), to its 2.625% Convertible Senior Debentures due 2025 (the 2025 Debentures) and 1.75% Convertible Senior Debentures due 2026 (the 2026 Debentures). Prior to the adoption of FSP APB 14-1, WESCO accounted for its convertible debt instruments solely as long-term debt. FSP APB 14-1 requires an issuer of certain convertible debt instruments to separately account for the liability and equity components of convertible debt instruments in a manner that reflects the issuer s nonconvertible debt borrowing rate. This accounting treatment results in an increase in non-cash interest reported in the financial statements, a decrease in long-term debt, an increase in equity and an increase in deferred income taxes.

As of March 31, 2009 and December 31, 2008, $150 million in aggregate principal amount of the 2025 Debentures was outstanding and $300 million in aggregate principal amount of the 2026 Debentures was outstanding. As of March 31, 2009, the unamortized discount for the 2025 Debentures and 2026 Debentures was $6.9 million and $29.7 million, respectively. As of December 31, 2008, the unamortized discount for the 2025 Debentures and 2026 Debentures was $8.1 million and $32.4 million, respectively. The net carrying amounts of the liability components are classified as long-term debt in the consolidated balance sheets. The debt discounts are being amortized over a five-year period starting on the dates of issuance. The amortization period ends on October 15, 2010 for the 2025 Debentures and November 15, 2011 for the 2026 Debentures. As of March 31, 2009 and December 31, 2008, the aggregate equity component for the 2025 Debentures and 2026 Debentures totaled $12.3 million and $31.2 million, respectively.

In accordance with SFAS No. 109, *Accounting for Income Taxes*, WESCO recorded a deferred tax liability for the basis difference associated with the liability components. The initial recognition of deferred taxes was recorded as an adjustment to additional capital. In subsequent periods, the deferred tax liability is reduced and a deferred tax benefit is recognized in earnings as the debt discount is amortized to pre-tax income.

Interest expense for the 2025 Debentures and 2026 Debentures totaled $6.1 million and $5.9 million for the three months ended March 31, 2009 and 2008, respectively, of which $3.8 million and $3.6 million, respectively, was non-cash interest. Interest was calculated using an effective interest rate of 6.0%.

The following table provides the effect of applying FSP APB 14-1 on individual line items in the 2008 financial statements:

Condensed Consolidated Balance Sheet	**Previously Reported December 31, 2008**	**Revised December 31, 2008**
Other assets	$ 29,562	$ 28,446
Total assets	2,720,977	2,719,861
Long-term debt	841,928	801,427
Deferred income taxes	120,459	136,736
Total liabilities	1,988,981	1,964,757
Additional capital	842,537	886,019

Retained earnings	497,485	477,111
Total stockholders equity	731,996	755,104
Total liabilities and stockholders equity	2,720,977	2,719,861

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Condensed Consolidated Statement of Income	Previously Reported Three Months Ended March 31, 2008	Revised Three Months Ended March 31, 2008
Interest expense, net	$ 14,563	$ 18,082
Income before income taxes	65,254	61,735
Provision for income taxes	20,424	19,045
Net Income	44,830	42,690
Earnings per share:		
Basic	1.05	1.00
Diluted	1.02	0.97

Condensed Consolidated Statement of Cash Flows	Three Months Ended March 31, 2008	Three Months Ended March 31, 2008
Net income	$ 44,830	$ 42,690
Adjustments to net income:		
Amortization of debt issuance costs	948	839
Amortization of debt discount		3,628
Deferred income taxes		(1,379)
Net cash provided by operating activities	91,961	91,961

4. STOCK-BASED COMPENSATION

WESCO s stock-based employee compensation plans are comprised of stock options and stock-settled stock appreciation rights. Beginning January 1, 2006, WESCO adopted SFAS No. 123 (revised 2004), *Share-Based Payment* (SFAS 123R), using the modified prospective method. Under SFAS 123R, compensation cost for all stock-based awards is measured at fair value on the date of grant and compensation cost is recognized, net of estimated forfeitures, over the service period for awards expected to vest. The fair value of stock-based awards is determined using the Black-Scholes valuation model. The forfeiture assumption is based on WESCO s historical employee behavior that is reviewed on an annual basis. No dividends are assumed.

There were no stock-settled stock appreciation rights granted during the three months ended March 31, 2009. During the three months ended March 31, 2008, WESCO granted the following stock-settled stock appreciation rights at the following weighted average assumptions:

	Three Months Ended March 31, 2008
Stock-settled appreciations rights granted	1,800
Risk free interest rate	2.5%
Expected life	4 years
Expected volatility	38%

For the three months ended March 31, 2008, the weighted average fair value per equity award granted was approximately $13.03.

WESCO recognized $3.2 million of non-cash stock-based compensation expense, which is included in selling, general and administrative expenses, for the three months ended March 31, 2009 and 2008. As of March 31, 2009, there was $15.4 million of total unrecognized compensation cost related to non-vested stock-based compensation arrangements for all awards previously made, of which approximately $7.3 million is expected to be recognized over the remainder of 2009, $6.1 million in 2010, and $2.0 million in 2011.

During the three months ended March 31, 2009 and 2008, the total intrinsic value of awards exercised was $0.2 million and $5.5 million, respectively, and the total amount of cash received from the exercise of options was $0.1 million and $2.2 million, respectively. The tax benefit associated with the exercise of awards for the three months ended March 31, 2009 and 2008 totaled $0.1 million and $1.6 million, respectively, and was recorded as a credit to additional paid-in capital.

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The following table sets forth a summary of both stock options and stock-settled appreciation rights and related information for the three months ended March 31, 2009:

	Awards	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (In Years)	Aggregate Intrinsic Value (In Thousands)
Outstanding at December 31, 2008	3,933,035	$ 36.44		
Granted				
Exercised	(20,000)	7.25		
Forfeited	(53,062)	45.59		
Outstanding at March 31, 2009	3,859,973	36.46	6.6	$ 6,653
Exercisable at March 31, 2009	2,421,732	$ 29.56	5.3	$ 6,640

5. EARNINGS PER SHARE

Basic earnings per share are computed by dividing net income by the weighted average common shares outstanding during the periods. Diluted earnings per share are computed by dividing net income by the weighted average common shares and common share equivalents outstanding during the periods. The dilutive effect of common share equivalents is considered in the diluted earnings per share computation using the treasury stock method, which includes consideration of stock-based compensation required by SFAS No. 123R and SFAS No. 128, *Earnings Per Share*.

The following table sets forth the details of basic and diluted earnings per share:

Amounts in thousands, except share and per share data	Three Months Ended March 31, 2009	Three Months Ended March 31, 2008
Net income reported[(1)]	$ 23,262	$ 42,690
Weighted average common shares outstanding used in computing basic earnings per share	42,246,795	42,741,818
Common shares issuable upon exercise of dilutive stock options	317,395	1,291,654
Weighted average common shares outstanding and common share equivalents used in computing diluted earnings per share	42,564,190	44,033,472
Earnings per share: [(1)]		
Basic	$ 0.55	$ 1.00
Diluted	$ 0.55	$ 0.97

(1) As a result of the retrospective application of

FSP ABP 14-1 on January 1, 2009, net income and earnings per share were revised for the three months ended March 31, 2008 (see Note 3 Accounting for Convertible Debt Instruments).

For the three months ended March 31, 2009 and 2008, the computation of diluted earnings per share excluded stock-settled stock appreciation rights of approximately 3.1 million and 1.1 million, respectively, at weighted average exercise prices of $43 per share and $63 per share, respectively. These amounts were excluded because their effect would have been antidilutive.

Under EITF Issue No. 04-8, *The Effect of Contingently Convertible Instruments on Diluted Earnings Per Share*, and EITF Issue No. 90-19*, Convertible Bonds with Issuer Option to Settle for Cash upon Conversion*, and because of WESCO s obligation to settle the par value of the 2025 Debentures and the 2026 Debentures (collectively, the Debentures) in cash, WESCO is not required to include any shares underlying the Debentures in its diluted weighted average shares outstanding until the average stock price per share for the period exceeds the conversion price of the respective Debentures. At such time, only the number of shares that would be issuable (under the treasury stock method of accounting for share dilution) would be included, which is based upon the amount by which the average stock price exceeds the conversion price. The conversion prices of the 2026 Debentures and 2025 Debentures are $88.15 and $41.86, respectively. Share dilution is limited to a maximum of 3,403,110 shares for the 2026 Debentures and 3,583,080 shares for the 2025 Debentures. Since the average stock price for the three month periods ended March 31, 2009 and 2008 was less than the conversion prices, there was no impact of the Debentures on diluted earnings per share.

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6. EQUITY INVESTMENT

During the first quarter of 2008, WESCO and Deutsch Engineering Connecting Devices, Inc. (Deutsch) completed a transaction with respect to WESCO s LADD operations, which resulted in a joint venture in which Deutsch owns a 60% interest and WESCO owns a 40% interest. Deutsch paid to WESCO aggregate consideration of approximately $75 million, consisting of $60 million in cash plus a $15 million promissory note, which is included in other accounts receivable in the consolidated balance sheet. Deutsch is entitled, but not obliged, to acquire the remaining 40% after January 1, 2010. As a result of this transaction, WESCO recognized an after-tax loss of approximately $2.1 million during the first quarter of 2008. WESCO accounts for its investment in the joint venture using the equity method of accounting as prescribed by Accounting Principles Board No. 18, *The Equity Method of Accounting for Investments in Common Stock*. Accordingly, earnings from the joint venture are recorded as other income in the consolidated statement of income.

7. EMPLOYEE BENEFIT PLANS

A majority of WESCO s employees are covered by defined contribution retirement savings plans for their services rendered subsequent to WESCO s formation. WESCO also offers a deferred compensation plan for select individuals. For U.S. participants, WESCO will make contributions in an amount equal to 50% of the participant s total monthly contributions up to a maximum of 6% of eligible compensation. For Canadian participants, WESCO will make contributions in an amount ranging from 1% to 7% of the participant s eligible compensation based on years of continuous service. In addition, employer contributions may be made at the discretion of the Board of Directors. For the three months ended March 31, 2009 and 2008, WESCO incurred charges of $5.4 million and $5.8 million, respectively, for all such plans. Contributions are made in cash to employee retirement savings plan accounts. Employees then have the option to transfer balances allocated to their accounts into any of the available investment options, including WESCO common stock.

8. COMMITMENTS AND CONTINGENCIES

WESCO is a co-defendant in a lawsuit filed in a state court in Indiana in which a customer alleges that WESCO sold defective products manufactured or remanufactured by others and is seeking monetary damages in the amount of $52 million. WESCO has denied any liability, believes that it has meritorious defenses and intends to vigorously defend itself against these allegations. Accordingly, no liability is recorded for this matter as of March 31, 2009.

9. COMPREHENSIVE INCOME

The following tables set forth comprehensive income and its components:

	Three Months Ended March 31,	
Amounts in thousands	**2009**	**2008** [(1)]
Net income	$ 23,262	$ 42,690
Foreign currency translation adjustment	(6,006)	(6,757)
Comprehensive income	$ 17,256	$ 35,933

(1) As a result of the retrospective application of FSP ABP 14-1 on January 1, 2009, net income and comprehensive income were revised for the

three months ended March 31, 2008 (see Note 3 Accounting for Convertible Debt Instruments).

10. SHARE REPURCHASE PLAN

On September 28, 2007, WESCO announced that its Board of Directors authorized a stock repurchase program in the amount of up to $400 million with an expiration date of September 30, 2009. The shares may be repurchased from time to time in the open market or through privately negotiated transactions. The stock repurchase program may be implemented or discontinued at any time by WESCO. No shares were repurchased during the three months ended March 31, 2009.

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11. INCOME TAXES

The following table sets forth the reconciliation between the federal statutory income tax rate and the effective rate:

	Three Months Ended March 31, 2009	Three Months Ended March 31, 2008 [2]
Federal statutory rate	35.0%	35.0%
State taxes, net of federal tax benefit	3.0	2.6
Nondeductible expenses	0.4	0.5
Domestic tax benefit from foreign operations	(0.9)	(0.5)
Foreign tax rate differences[1]	(8.1)	(6.4)
Domestic production activity deduction	(0.3)	(0.2)
Adjustment related to uncertain tax positions	0.4	(0.5)
Other	(0.8)	0.3
	28.7%	30.8%

(1) Includes a benefit of $2.4 million and $3.5 million for the three months ended March 31, 2009 and 2008, respectively, from the recapitalization of Canadian operations.

(2) As a result of the retrospective application of FSP ABP 14-1 on January 1, 2009, the effective rate was revised for the three months ended March 31, 2008 (see Note 3 Accounting for Convertible Debt Instruments).

In accordance with FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109,* WESCO analyzes its filing positions for all open tax years in all jurisdictions. The Company is currently under examination in several tax jurisdictions, both within the United States and outside the United States, and remains subject to examination until the statute of limitations expires for the respective tax jurisdictions. The following summary sets forth the tax years that remain open in the Company s major tax jurisdictions:

United States Federal	2000 and forward
United States States	2004 and forward
Canada	1996 and forward

During the next twelve months, it is reasonably possible that certain issues will be settled by the resolution of Internal Revenue Service tax examinations or the expiration of statutes of limitations. An estimate of the amount of change in unrecognized tax benefits cannot be made at this time as the outcome of the audits and the timing of the settlements are subject to significant uncertainty.

The total amounts of unrecognized tax benefits were $7.7 million and $7.5 million as of March 31, 2009 and December 31, 2008, respectively. If these tax benefits were recognized in the consolidated financial statements, the portion of these amounts that would reduce the Company s effective tax rate would be $6.5 million and $6.3 million, respectively. WESCO records interest related to uncertain tax positions as a part of interest expense in the consolidated statement of income. Any penalties are recognized as part of income tax expense. As of March 31, 2009 and December 31, 2008, WESCO had an accrued liability of $3.7 million and $3.5 million, respectively, for interest related to uncertain tax positions. There were no penalties recorded during the three months ended March 31, 2009.

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12. OTHER FINANCIAL INFORMATION

WESCO Distribution, Inc. (WESCO Distribution) has outstanding $150 million in aggregate principal amount of 7.50% Senior Subordinated Notes due 2017 (the 2017 Notes), and WESCO International, Inc. has outstanding $150 million in aggregate principal amount of 2025 Debentures and $300 million in aggregate principal amount of 2026 Debentures. The 2017 Notes are fully and unconditionally guaranteed by WESCO International, Inc. on a subordinated basis to all existing and future senior indebtedness of WESCO International, Inc. The 2025 Debentures and 2026 Debentures are fully and unconditionally guaranteed by WESCO Distribution, on a senior subordinated basis to all existing and future senior indebtedness of WESCO Distribution.

Condensed consolidating financial information for WESCO International, Inc., WESCO Distribution and the non-guarantor subsidiaries is as follows:

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WESCO INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATING BALANCE SHEETS

	March 31, 2009 (In thousands)				
	WESCO International, Inc.	WESCO Distribution, Inc.	Non-Guarantor Subsidiaries	Consolidating and Eliminating Entries	Consolidated
Cash and cash equivalents	$ (2)	$ 26,190	$ 78,947	$	$ 105,135
Trade accounts receivable, net			687,801		687,801
Inventories, net		389,228	171,842		561,070
Other current assets	(12,297)	61,053	30,174		78,930
Total current assets	(12,299)	476,471	968,764		1,432,936
Intercompany receivables, net		(1,418,159)	1,905,635	(487,476)	
Property, buildings and equipment, net		45,703	71,156		116,859
Intangible assets, net		9,338	77,436		86,774
Goodwill and other intangibles, net		395,545	467,465		863,010
Investments in affiliates and other noncurrent assets	1,688,807	3,075,198	17,944	(4,708,826)	73,123
Total assets	$1,676,508	$ 2,584,096	$3,508,400	$(5,196,302)	$2,572,702
Accounts payable	$	$ 401,285	$ 122,976	$	$ 524,261
Short-term debt			245,000		245,000
Other current liabilities		34,994	72,622		107,616
Total current liabilities		436,279	440,598		876,877
Intercompany payables, net	487,476			(487,476)	
Long-term debt	413,337	302,942	40,922		757,201
Other noncurrent liabilities		160,758	2,171		162,929
Stockholders equity	775,695	1,684,117	3,024,709	(4,708,826)	775,695
Total liabilities and stockholders equity	$1,676,508	$ 2,584,096	$3,508,400	$(5,196,302)	$2,572,702

December 31, 2008 (1)
(In thousands)

	WESCO International, Inc.	WESCO Distribution, Inc.	Non-Guarantor Subsidiaries	Consolidating and Eliminating Entries	Consolidated
Cash and cash equivalents	$	$ 18,453	$ 67,885	$	$ 86,338
Trade accounts receivable, net			791,356		791,356
Inventories, net		421,178	184,500		605,678
Other current assets	(12,100)	44,469	41,922		74,291
Total current assets	(12,100)	484,100	1,085,663		1,557,663
Intercompany receivables, net		(1,367,199)	1,862,220	(495,021)	
Property, buildings and equipment, net		46,389	72,834		119,223
Intangible assets, net		9,549	79,140		88,689
Goodwill and other intangibles, net		395,546	467,232		862,778
Investments in affiliates and other noncurrent assets	1,671,724	3,074,554	19,133	(4,673,903)	91,508
Total assets	$1,659,624	$ 2,642,939	$3,586,222	$(5,168,924)	$2,719,861
Accounts payable	$	$ 445,346	$ 126,486	$	$ 571,832
Short-term debt			295,000		295,000
Other current liabilities		69,076	70,101		139,177
Total current liabilities		514,422	491,587		1,006,009
Intercompany payables, net	495,021			(495,021)	
Long-term debt	409,499	350,601	41,327		801,427
Other noncurrent liabilities		111,422	45,899		157,321
Stockholders equity	755,104	1,666,494	3,007,409	(4,673,903)	755,104
Total liabilities and stockholders equity	$1,659,624	$ 2,642,939	$3,586,222	$(5,168,924)	$2,719,861

(1) The balances reported as of December 31, 2008 have been revised as a result of the retrospective application of FSP ABP 14-1

on January 1, 2009 (see Note 3 Accounting for Convertible Debt Instruments).

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WESCO INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATING STATEMENTS OF INCOME

	Three Months Ended March 31, 2009 (In thousands)				
	WESCO International, Inc.	WESCO Distribution, Inc.	Non-Guarantor Subsidiaries	Consolidating and Eliminating Entries	Consolidated
Net sales	$	$ 834,870	$344,720	$	$1,179,590
Cost of goods sold		672,681	268,732		941,413
Selling, general and administrative expenses	2	145,689	41,798		187,489
Depreciation and amortization		3,595	3,562		7,157
Results of affiliates operations	23,629	17,300		(40,929)	
Interest expense, net	365	3,522	8,631		12,518
Other income		(1,626)			(1,626)
Provision for income taxes		4,680	4,697		9,377
Net income	$23,262	$ 23,629	$ 17,300	$ (40,929)	$ 23,262

	Three Months Ended March 31, 2008 [1] (In thousands)				
	WESCO International, Inc.	WESCO Distribution, Inc.	Non-Guarantor Subsidiaries	Consolidating and Eliminating Entries	Consolidated
Net sales	$	$1,035,513	$429,693	$	$1,465,206
Cost of goods sold		836,481	333,080		1,169,561
Selling, general and administrative expenses	2	169,643	41,994		211,639
Depreciation and amortization		3,775	3,158		6,933
Results of affiliates operations	39,240	35,407		(74,647)	
Interest (income) expense, net	(3,452)	9,808	11,726		18,082
Other income		(2,744)			(2,744)
Provision for income taxes		14,717	4,328		19,045
Net income	$42,690	$ 39,240	$ 35,407	$ (74,647)	$ 42,690

[1] The balances reported for the

three months ended March 31, 2008 have been revised as a result of the retrospective application of FSP ABP 14-1 on January 1, 2009 (see Note 3 Accounting for Convertible Debt Instruments).

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WESCO INTERNATIONAL, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATING STATEMENTS OF CASH FLOWS

	Three Months Ended March 31, 2009 (In thousands)				
	WESCO International, Inc.	WESCO Distribution, Inc.	Non-Guarantor Subsidiaries	Consolidating and Eliminating Entries	Consolidated
Net cash provided by operating activities	$ 7,369	$ 112,978	$ 14,247	$	$ 134,594
Investing activities:					
Capital expenditures		(2,663)	(193)		(2,856)
Acquisition payments		(74)			(74)
Other		82			82
Net cash used by investing activities		(2,655)	(193)		(2,848)
Financing activities:					
Net repayments	(7,545)	(89,955)	(371)		(97,871)
Equity transactions	174				174
Other		(12,631)			(12,631)
Net cash used by financing activities	(7,371)	(102,586)	(371)		(110,328)
Effect of exchange rate changes on cash and cash equivalents			(2,621)		(2,621)
Net change in cash and cash equivalents	(2)	7,737	11,062		18,797
Cash and cash equivalents at the beginning of year		18,453	67,885		86,338
Cash and cash equivalents at the end of period	$ (2)	$ 26,190	$ 78,947	$	$ 105,135

	Three Months Ended March 31, 2008[1] (In thousands)				
	WESCO International, Inc.	WESCO Distribution, Inc.	Non-Guarantor Subsidiaries	Consolidating and Eliminating Entries	Consolidated
	$(10,953)	$ 78,649	$ 24,265	$	$ 91,961

Net cash (used) provided by operating activities					
Investing activities:					
Capital expenditures		(11,034)	(285)		(11,319)
Acquisition payments		(96)			(96)
Proceeds from sale of subsidiary		60,000			60,000
Other		13			13
Net cash provided (used) by investing activities		48,883	(285)		48,598
Financing activities:					
Net borrowings (repayments)	32,088	(111,383)	(338)		(79,633)
Equity transactions	(21,132)				(21,132)
Other		(15,361)			(15,361)
Net cash provided (used) by financing activities	10,956	(126,744)	(338)		(116,126)
Effect of exchange rate changes on cash and cash equivalents			(2,298)		(2,298)
Net change in cash and cash equivalents	3	788	21,344		22,135
Cash and cash equivalents at the beginning of year	(7)	32,140	40,164		72,297
Cash and cash equivalents at the end of period	$ (4)	$ 32,928	$ 61,508	$	$ 94,432

(1) The balances reported for net cash (used) provided by operating activities for the three months ended March 31, 2008 have been revised as a result of the retrospective application of FSP ABP 14-1 on January 1, 2009 (see Note 3 Accounting for Convertible Debt Instruments).

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SUBSEQUENT EVENT

On April 13, 2009, WESCO Distribution entered into an amendment and restatement of its existing accounts receivable securitization facility (the Receivables Facility), pursuant to the terms and conditions of the Third Amended and Restated Receivables Purchase Agreement, dated as of April 13, 2009 (the Restated Agreement), by and among WESCO Receivables Corp., WESCO Distribution the Purchasers and Purchaser Agents party thereto and PNC Bank, National Association (as successor to Wachovia Capital Markets, LLC), as Administrator. The Restated Agreement decreases the purchase commitment under the Receivables Facility from $500 million to $400 million, subject to the right of WESCO Distribution to increase the purchase commitment from time to time up to $450 million with the voluntary participation of existing Purchasers and/or the addition of new Purchasers to fund such increase. The Restated Agreement also extends the term of the Receivables Facility to April 13, 2012; accordingly, we anticipate that outstanding borrowings under the Receivables Facility could be classified as long-term debt in the consolidated balance sheet in subsequent periods. The outstanding borrowings as of March 31, 2009 and December 31, 2008 are classified as short-term debt because prior to the Restated Agreement third party conduits and financial institutions could under certain conditions require WESCO Distribution to repay all or a portion of the outstanding amount.

Under the Receivables Facility, WESCO Distribution sells, on a continuous basis, an undivided interest in all domestic accounts receivable to WESCO Receivables Corp., a wholly-owned special purpose entity (the SPE). The SPE sells, without recourse, a senior undivided interest in the receivables to third-party conduits and financial institutions for cash while maintaining a subordinated undivided interest in the receivables, in the form of overcollateralization. WESCO Distribution has agreed to continue servicing the sold receivables for the third-party conduits and financial institutions at market rates; accordingly, no servicing asset or liability has been recorded.

As of March 31, 2009 and December 31, 2008, accounts receivable eligible for securitization totaled $496.8 million and $602.9 million, respectively. The consolidated balance sheets as of March 31, 2009 and December 31, 2008 reflect $245.0 million and $295.0 million, respectively, of account receivable balances legally sold to third parties, as well as borrowings for equal amounts. At March 31, 2009, the interest rate on borrowings under this facility was approximately 1.6%.

Item 2. Management s Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with the information in the unaudited condensed consolidated financial statements and notes thereto included herein and WESCO International Inc. s Financial Statements and Management s Discussion and Analysis of Financial Condition and Results of Operations included in its 2008 Annual Report on Form 10-K.

Company Overview

We are a full-line distributor of electrical supplies and equipment and a provider of integrated supply procurement services. We have approximately 400 full service branches and seven distribution centers located in the United States, Canada, Mexico, the United Kingdom, Nigeria, United Arab Emirates, Singapore, Australia and China. We serve approximately 115,000 customers worldwide, offering over 1,000,000 products from more than 23,000 suppliers. Our diverse customer base includes a wide variety of industrial companies; contractors for industrial, commercial and residential projects; utility companies, and commercial, institutional and governmental customers. Approximately 85% of our net sales are generated from operations in the United States, 11% from Canada and the remainder from other countries.

Our financial results for the first three months of 2009 reflect weak conditions in our markets served, along with unfavorable foreign currency exchange rates and the negative impact of lower commodity prices. Sales decreased $285.6 million, or 19.5%, over the same period last year. Cost of goods sold as a percentage of net sales was 79.8% for the first three months of 2009 and 2008. Operating income decreased by $33.5 million, or 43.5%, primarily from the decrease in sales resulting from the decline in end market activity. Net income for the three months ended March 31, 2009 and 2008 was $23.3 million and $42.7 million, respectively.

Cash Flow

We generated $134.6 million in operating cash flow for the first three months of 2009. Included in this amount was net income of $23.3 million and a decrease in trade and other receivables of $113.9 million. Investing activities were primarily comprised of capital expenditures which totaled $2.9 million for the first three months of 2009. Financing activities consisted of borrowings and repayments of $71.0 million and $118.5 million, respectively, related to our revolving credit facility, and net repayments of $50.0 million related to our Receivables Facility, whereby we sell, on a continuous basis, an undivided interest in all domestic accounts receivable to WESCO Receivables Corp., a wholly owned SPE.

Financing Availability

As of March 31, 2009, we had $300.9 million in total available borrowing capacity. The available borrowing capacity under our revolving credit facility was $151.9 million, of which $86.5 million is the U.S. sub-facility borrowing limit and $65.4 million is the Canadian sub-facility borrowing limit. The revolving credit facility does not mature until November 1, 2013. The available borrowing capacity under the Receivables Facility, which was amended and restated on April 13, 2009, was $149.0 million. The Receivables Facility matures on April 13, 2012. In addition, our 2025 Debentures and 2026 Debentures cannot be redeemed or repurchased until October 2010 and November 2011, respectively. We increased our cash by $18.8 million to $105.1 million, after taking into account $98.6 million of net debt repayments and $2.9 million of capital expenditures. We monitor the depository institutions that hold our cash and cash equivalents on a regular basis, and we believe that we have placed our deposits with creditworthy financial institutions. For further discussion refer to Liquidity and Capital Resources.

Outlook

We believe that improvements made to our operations and capital structure and actions taken in 2008 and the first quarter of 2009, including the amendment and restatement of the accounts receivable securitization facility in April, have helped position the Company to operate effectively in the lower level of activity being experienced in our end markets.. Current macroeconomic data and input from internal sales management, customers, and suppliers suggest activity levels in our major end markets will continue to be significantly weaker in 2009. Despite anticipated weakness, we believe that our opportunity pipeline remains strong. We believe that our strong market position, broad portfolio of products and services, and extensive information technology platform, combined with our continued focus on selling and marketing programs, margin improvement, and productivity initiatives, should provide us with a competitive advantage in the market.

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Critical Accounting Policies and Estimates

Our critical accounting policies are described in the notes to our consolidated financial statements for the year ended December 31, 2008 contained in our Annual Report on Form 10-K. Any new accounting policies or updates to existing accounting policies as a result of new accounting pronouncements have been included in the notes to our Condensed Consolidated Financial Statements for the period ended March 31, 2009.

Results of Operations

First Quarter of 2009 versus First Quarter of 2008

The following table sets forth the percentage relationship to net sales of certain items in our condensed consolidated statements of income for the periods presented:

	Three Months Ended March 31,	
	2009	**2008**[(1)]
Net sales	100.0%	100.0%
Cost of goods sold	79.8	79.8
Selling, general and administrative expenses	15.9	14.4
Depreciation and amortization	0.6	0.5
Income from operations	3.7	5.3
Interest expense	1.0	1.2
Other income	(0.1)	(0.1)
Income before income taxes	2.8	4.2
Provision for income taxes	0.8	1.3
Net income	2.0%	2.9%

(1) As a result of the retrospective application of FSP ABP 14-1 on January 1, 2009, interest expense, income before income taxes, provision for income taxes and net income were revised for the three months ended March 31, 2008 (see Note 3 to the consolidated financial statements).

Net sales in the first quarter of 2009 totaled $1,179.6 million versus $1,465.2 million in the comparable period for 2008, a decrease of $285.6 million, or 19.5%, over the same period last year. Sales were negatively impacted by weak market conditions, unfavorable foreign currency exchange rates, lower commodity prices and one less workday in the first quarter 2009 compared to the same period in 2008.

Cost of goods sold for the first quarter of 2009 was $941.4 million versus $1,169.6 million for the comparable period in 2008, and cost of goods sold as a percentage of net sales was 79.8% in 2009 and 2008. The cost of goods sold percentage was equivalent to the first quarter of 2008 due to effective pricing and procurement initiatives which more than offset the decrease in commodity prices and an unfavorable sales mix.

Selling, general and administrative (SG&A) expenses in the first quarter of 2009 totaled $187.5 million versus $211.6 million in last year s comparable quarter. The decrease in SG&A expenses is due to aggressive cost reductions actions. As a percentage of net sales, SG&A expenses were 15.9% in the first quarter of 2009 compared to 14.4% in the first quarter of 2008, reflecting a decrease in sales volume.

SG&A payroll expenses for the first quarter of 2009 of $131.6 million decreased by $13.5 million compared to the same quarter in 2008. The decrease in payroll expenses was primarily due to a decrease in salaries and wages of $6.2 million, a decrease in incentive costs of $3.0 million, a decrease in benefit costs of $1.9 million and a decrease in temporary labor costs of $1.5 million. Other SG&A related payroll expenses decreased $0.9 million.

The remaining SG&A expenses for the first quarter of 2009 of $55.9 million decreased by approximately $10.6 million compared to same quarter in 2008. Included in this period s SG&A expenses was a decrease in transportation costs of $2.9 million due to the decrease in sales volume, a decrease in travel costs of $1.9 million and a decrease in bad debt expense of $1.6 million due to a specific customer default recognized in last year s comparable period. Other SG&A expenses decreased $4.2 million.

Depreciation and amortization for the first quarter of 2009 was $7.2 million versus $6.9 million in last year s comparable quarter. The increase is due to the $35.3 million of capital expenditures in the prior year.

Interest expense totaled $12.5 million for the first quarter of 2009 versus $18.1 million in last year s comparable quarter, a decrease of 30.8%. Interest expense for the first quarter of 2009 was primarily impacted by the reduction in interest rates and the decrease in debt. On January 1, 2009, we retrospectively applied the provisions of FSP APB 14-1, *Accounting for Convertible Debt Instruments That May Be Settled in Cash Upon Conversion (Including Partial Cash Settlement)* (FSP APB 14-1), for our 2.625% Convertible Senior Debentures due 2025 (the 2025 Debentures) and 1.75% Convertible Senior Debentures due 2026 (the 2026 Debentures). This change in accounting treatment results in an increase in non-cash interest reported in the financial statements, a decrease in long-term debt, an increase in equity and an increase in deferred income taxes Interest expense for the 2025 Debentures and 2026 Debentures totaled $6.1 million and $5.9 million for the three months ended March 31, 2009 and 2008, respectively, of which $3.8 million and $3.6 million, respectively, was non-cash interest.

Other income totaled $1.6 million for the first quarter of 2009 versus $2.7 million in the comparable period for 2008. We account for our investment in the LADD joint venture on an equity basis, and earnings are reported as other income in the consolidated statement of income. The decrease in other income is primarily due to the decrease in the joint venture s income.

Income tax expense totaled $9.4 million in the first quarter of 2009, and the effective tax rate was 28.7% compared to 30.8% in the same quarter in 2008. The decrease in the effective tax rate is primarily a result of a lower tax rate from foreign operations.

For the first quarter of 2009, net income decreased by $19.4 million to $23.3 million compared to $42.7 million in the first quarter of 2008. Diluted earnings per share was $0.55 for the first quarter of 2009 compared with $0.97 per diluted share for the first quarter of 2008. The decrease in net income was primarily due to the decline in sales attributable to the weak market conditions.

Liquidity and Capital Resources

Total assets were $2.6 billion at March 31, 2009, compared to $2.7 billion at December 31, 2008. The $147.2 million decrease in total assets was principally attributable to the decrease in accounts receivable and inventory of $103.6 million and $44.6 million, respectively. These reductions were due to the decrease in sales activity. Total liabilities at March 31, 2009 compared to December 31, 2008 decreased by $167.8 million to $1.8 billion. Contributing to the decrease in total liabilities was a decrease in short-term and long-term debt of $94.2 million; a decrease in accounts payable of $47.6 million due to reduced purchasing activity; a decrease in accrued payroll and benefit costs of $16.1 million due to the payment of the 2008 management incentive compensation; and a decrease in bank overdrafts of $11.9 million. Stockholders equity increased 2.7% to $775.7 million at March 31, 2009, compared with $755.1 million at December 31, 2008, primarily as a result of net earnings of $23.3 million and stock-based compensation expense of $3.2 million. These increases were partially offset by foreign currency translation adjustments of $6.0 million.

A possible indicator of impairment is the relationship of a company s market capitalization to its book value. As of March 31, 2009, our market capitalization exceeded our book value. The persistence or further acceleration of the recent downturn in the global economic conditions and turbulence in financial markets could have a further negative impact on our market capitalization and/or financial performance. Our recent large acquisitions are most sensitive to a decline in financial performance. Therefore, we cannot predict whether or not there will be certain events that could adversely affect the reported value of goodwill and trademarks, which totaled $900.9 million and $900.7 million at March 31, 2009 and December 31, 2008, respectively.

Our liquidity needs arise from working capital requirements, capital expenditures, acquisitions and debt service obligations. As of March 31, 2009, we had $151.9 million in available borrowing capacity under our revolving credit facility, which combined with our $149.0 million of available borrowing capacity under our Receivables Facility and our invested cash provides us with liquidity of $364.8 million. We believe cash provided by operations and financing activities will be adequate to cover our current operational and business needs.

The worldwide financial turmoil has had significant impacts on global credit markets. We communicate on a regular basis with our lenders regarding our financial and working capital performance and liquidity position. We are in compliance with all covenants and restrictions as of March 31, 2009. On April 13, 2009, we entered into a $400 million amended and restated receivables purchase agreement. As previously mentioned, the amended and restated Receivables Facility is not subject to renewal until April 2012. In addition, in October 2008 Moody s Investor Services and Standard & Poor s affirmed our credit rating and stable outlook.

Over the next several quarters we expect to maintain working capital productivity, and it is expected that excess cash will be directed primarily at debt reduction. Our near term focus will continue to be on our cost structure, right sizing of the business and maintaining ample liquidity and credit availability. We believe our balance sheet and ability to generate ample cash flow provides us with a durable business model and should allows us to fund expansion needs and growth initiatives in this time of economic contraction while maintaining targeted levels of leverage. To the extent that operating cash flow is materially lower than current levels or external financing sources are not available on terms competitive with those currently available, including increases in interest rates, future liquidity may be adversely affected.

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Cash Flow

Operating Activities. Cash provided by operating activities for the first three months of 2009 totaled $134.6 million compared with $92.0 million of cash generated for the first three months of 2008. Cash provided by operating activities in the first three months of 2009 included net income of $23.3 million and adjustments to net income totaling $18.5 million. The increased level of cash flow is primarily attributable to a decrease in trade and other receivables of $113.9 million resulting from the decrease in sales and a decrease in inventory of $42.9 million. Cash used by operating activities in the first three months of 2009 included: $45.4 million for the decrease in accounts payable, resulting from the decrease in purchasing activity; and $16.1 million for the decrease in accrued payroll and benefit costs, resulting from the payment of the 2008 management incentive compensation. In the first three months of 2008, primary sources of cash were net income of $42.7 million and adjustments to net income totaling $12.2 million; an inventory reduction of $26.9 million; and an accounts payable increase of $23.4 million, resulting from the increase in the cost of sales. Cash used by operating activities in the first three months of 2008 included $16.9 million for the increase in trade and other receivables, resulting from the increase in sales; and $14.5 million for the decrease in accrued payroll and benefit costs, resulting from the payment of the 2007 management incentive compensation.

Investing Activities. Net cash used by investing activities for the first three months of 2009 was $2.8 million, compared with $48.6 million of net cash provided during the first three months of 2008. Included in 2008 were proceeds of $60.0 million from the partial divestiture of the LADD operations. Capital expenditures were $2.9 million and $11.3 million in the first three months of 2009 and 2008, respectively. The decrease in capital expenditures in 2009 is due to cash management initiatives.

Financing Activities. Net cash used by financing activities for the first three months of 2009 and 2008 was $110.3 million and $116.1 million, respectively. During the first three months of 2009, borrowings and repayments of long-term debt of $71.0 million and $118.5 million, respectively, were made to our revolving credit facility. Borrowings and repayments of $55.0 million and $105.0 million, respectively, were applied to our Receivables Facility, and there were repayments of $0.4 million to our mortgage financing facility. During the first three months of 2008, borrowings and repayments of long-term debt of $241.5 million and $323.8 million, respectively, were made to our revolving credit facility. Borrowings and repayments of $83.0 million and $80.0 million, respectively, were applied to our Receivables Facility, and there were repayments of $0.3 million to our mortgage financing facility. In addition, during the first three months of 2008, we purchased shares of our common stock under our share repurchase plan for approximately $24.9 million. The exercise of stock-based compensation arrangements resulted in proceeds of $0.1 million and $2.2 million during the first three months of 2009 and 2008, respectively.

Contractual Cash Obligations and Other Commercial Commitments

There were no material changes in our contractual obligations and other commercial commitments that would require an update to the disclosure provided in our 2008 Annual Report on Form 10-K other than the subsequent events disclosure in Note 13 to the condensed consolidated financial statements.. Management believes that cash generated from operations, together with amounts available under our revolving credit facility and the Receivables Facility, will be sufficient to meet our working capital, capital expenditures and other cash requirements for the foreseeable future. There can be no assurances, however, that this will be or will continue to be the case.

Inflation

The rate of inflation affects different commodities, the cost of products purchased and ultimately the pricing of our different products and product classes to our customers. As a result of the worldwide financial turmoil, we experienced price deflation during the three months ended March 31, 2009. On an overall basis, our pricing related to deflation comprised an estimated $25.0 million of our sales decline.

Seasonality

Our operating results are not significantly affected by certain seasonal factors. Sales during the first quarter are generally less than 2% below the sales of the remaining three quarters due to reduced level of activity during the winter months of January and February. Sales typically increase beginning in March with slight fluctuations per month through December.

Impact of Recently Issued Accounting Standards

In September 2006, the Financial Accounting Standards Board (the FASB) issued Statement of Financial Accounting Standards (SFAS) No. 157, *Fair Value Measurements* (SFAS 157) which defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. This statement applies whenever other accounting standards require or permit assets or liabilities to be measured at fair value but does not expand the use of fair value to new accounting transactions and does not apply to pronouncements that address share-based payment transactions. On February 12, 2008, the FASB issued FASB Staff Position (FSP) SFAS No. 157-2, Effective Date of SFAS No. 157. The FSP amends SFAS 157 to delay the effective date of SFAS 157 for all nonfinancial assets and liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis (that is, at least annually) to fiscal years beginning after November 15, 2008. Except for the delay for nonfinancial assets and liabilities, SFAS 157 was effective for fiscal years beginning after November 15, 2007. Consistent with its requirements, we adopted SFAS 157 for our financial assets and liabilities on January 1, 2008. Our financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable, bank overdrafts and debt. We believe that the recorded values of our financial instruments, except for long-term debt, approximate fair value because of their nature and respective duration. The partial adoption of SFAS 157 did not impact our financial position, results of operations, or cash flows. On January 1, 2009, we adopted SFAS 157 for our nonfinancial assets and liabilities which include those measured at fair value in goodwill and indefinite lived intangible asset impairment testing, and assets acquired and liabilities assumed in a business combination. The adoption of SFAS 157 for nonfinancial assets and liabilities did not impact our financial position, results of operations or cash flows. However, in the event that we acquire a new business or have an impairment issue related to goodwill or indefinite lived intangible assets, the determination of fair value of the assets and liabilities will be subject to SFAS 157.

In December 2007, the FASB issued SFAS No. 141 (revised 2007), *Business Combinations* (SFAS 141R) which establishes additional principles and requirements for how the acquirer in a business combination recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed and any noncontrolling interest in the acquiree at the acquisition date fair value. SFAS 141R is designed to improve the relevance, representational faithfulness, and comparability of the financial information that a reporting entity provides in its financial reports about a business combination and its effects. SFAS 141R applies prospectively to business combinations for which the acquisition date is in or after the beginning of the first annual reporting period beginning after December 15, 2008. As there were no acquisitions executed in the first quarter of 2009, the adoption of SFAS 141R did not impact our financial position, results of operations or cash flows.

In April 2008, the FASB issued FSP No. FAS 142-3, *Determination of the Useful Life of Intangible Assets* (FSP FAS 142-3) which amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under SFAS No. 142, *Goodwill and Other Intangible Assets* (SFAS 142), and requires additional disclosure. The objective of FSP FAS 142-3 is to improve the consistency between the useful life of a recognized intangible asset under SFAS 142 and the period of expected cash flows used to measure the fair value of the asset under SFAS 141R and other generally accepted accounting principles. FSP FAS 142-3 is effective for fiscal years beginning after December 15, 2008 and shall be applied prospectively to intangible assets acquired after the effective date. The adoption of FSP FAS 142-3 did not impact our financial position, results of operations or cash flows.

Forward-Looking Statements

From time to time in this report and in other written reports and oral statements, references are made to expectations regarding our future performance. When used in this context, the words anticipates, plans, believes, estimates, intends, expects, projects, will and similar expressions may identify forward-looking statements, altho not all forward-looking statements contain such words. Such statements including, but not limited to, our statements regarding our business strategy, growth strategy, productivity and profitability enhancement, new product and service introductions and liquidity and capital resources are based on management s beliefs, as well as on assumptions made by, and information currently available to, management, and involve various risks and uncertainties, certain of which are beyond our control. Our actual results could differ materially from those expressed in any forward-looking statement made by or on our behalf. In light of these risks and uncertainties there can be no assurance that the forward-looking information will in fact prove to be accurate. Factors that might cause actual results to differ from such forward-looking statements include, but are not limited to, an increase in competition, the amount of outstanding indebtedness, the availability of appropriate acquisition opportunities, availability of key products, functionality of information systems, international operating environments, global and national economic and market factors and other risks that are described in our Annual Report on Form 10-K for our fiscal year ended December 31, 2008, or other documents subsequently filed with the Securities and Exchange Commission. We have undertaken no obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

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Item 3. Quantitative and Qualitative Disclosures about Market Risks

There have not been any material changes to our exposures to market risk during the quarter ended March 31, 2009 that would require an update to the disclosures provided in our 2008 Annual Report on Form 10-K.

Item 4. Controls and Procedures

Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures

Under the supervision and with the participation of our management, including our principal executive officer and principal financial officer, we conducted an evaluation of our disclosure controls and procedures as such term is defined under Rule 13a-15(e) promulgated under the Exchange Act. Based on this evaluation, our principal executive officer and our principal financial officer concluded that our disclosure controls and procedures were effective as of the end of the period covered by this report.

Changes in Internal Control Over Financial Reporting

During the first quarter of 2009, there were no changes in our internal control over financial reporting identified in connection with management s evaluation of the effectiveness of our internal control over financial reporting that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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Part II Other Information
Item 1. Legal Proceedings

From time to time, a number of lawsuits and claims have been or may be asserted against us relating to the conduct of our business, including routine litigation relating to commercial and employment matters. The outcome of any litigation cannot be predicted with certainty, and some lawsuits may be determined adversely to us. However, management does not believe, based on information presently available, that the ultimate outcome of any such pending matters is likely to have a material adverse effect on our financial condition or liquidity, although the resolution in any quarter of one or more of these matters may have a material adverse effect on our results of operations for that period.

As previously reported in our Annual Report on Form 10-K, we are a co-defendant in a lawsuit filed in a state court in Indiana in which a customer alleges that we sold defective products manufactured or remanufactured by others and is seeking monetary damages in the amount of $52 million. We have denied any liability, continue to believe that we have meritorious defenses and ding-left:2px;padding-top:2px;padding-bottom:2px;">
4,771

5,260

Europe
17,170

19,630

South America
4,159

302

Total cash and cash equivalents
$
49,695

$
50,611

Restricted Cash

In connection with a court order issued in a now settled litigation matter, we previously placed $4.6 million of cash into a collateralized surety bond. This bond had certain restrictions for liquidation and was therefore classified as restricted cash. On February 10, 2017, the $4.6 million surety bond was returned to us upon final settlement of the related litigation matter.

In connection with the pending sale of our Guangzhou factory in the PRC (Note 10), the buyer made a cash deposit of RMB 32 million ($4.7 million based on June 30, 2017 exchange rates) into an escrow account on September 29, 2016. Under the terms of the escrow account, these funds will not be paid to us until the close of the sale. Accordingly, this deposit is presented as long-term restricted cash within our consolidated balance sheet.

Note 3 — Accounts Receivable, Net and Revenue Concentrations

Accounts receivable, net were as follows:

(In thousands)	June 30, 2017	December 31, 2016
Trade receivables, gross	$140,845	$ 120,965
Allowance for doubtful accounts	(950)	(904)
Allowance for sales returns	(480)	(539)
Net trade receivables	139,415	119,522
Other	8,323	5,070
Accounts receivable, net	$147,738	$ 124,592

Allowance for Doubtful Accounts

Changes in the allowance for doubtful accounts were as follows:

(In thousands)	Six Months Ended June 30,	
	2017	2016
Balance at beginning of period	$904	$822
Additions (reductions) to costs and expenses	81	116
(Write-offs)/Foreign exchange effects	(35)	4
Balance at end of period	$950	$942

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(Unaudited)

Sales Returns
The allowance for sales returns at June 30, 2017 and December 31, 2016 included reserves for items returned prior to period-end that were not completely processed, and therefore had not yet been removed from the allowance for sales returns balance. If these returns had been fully processed, the allowance for sales returns balance would have been approximately $0.2 million and $0.4 million on June 30, 2017 and December 31, 2016, respectively. The value of these returned goods was included in our inventory balance at June 30, 2017 and December 31, 2016.
Significant Customers
Net sales to the following customers totaled more than 10% of our net sales:

	Three Months Ended June 30,					
	2017			2016		
	$ (thousands)	% of Net Sales		$ (thousands)	% of Net Sales	
Comcast Corporation	$42,951	24.2	%	$36,366	21.3	%
DIRECTV	17,826	10.0		20,035	11.7	

	Six Months Ended June 30,					
	2017			2016		
	$ (thousands)	% of Net Sales		$ (thousands)	% of Net Sales	
Comcast Corporation	$85,198	25.1	%	$75,975	23.6	%
DIRECTV	34,458	10.2		36,854	11.5	

Trade receivables associated with these significant customers that totaled more than 10% of our accounts receivable, net were as follows:

	June 30, 2017			December 31, 2016		
	$ (thousands)	% of Accounts Receivable, Net		$ (thousands)	% of Accounts Receivable, Net	
Comcast Corporation	$30,491	20.6	%	$23,716	19.0	%
DIRECTV	15,718	10.6		12,878	10.3	

Note 4 — Inventories, Net and Significant Supplier
Inventories, net were as follows:

(In thousands)	June 30, 2017		December 31, 2016	
Raw materials	$40,035		$ 33,059	
Components	20,241		15,046	
Work in process	5,227		5,860	
Finished goods	82,121		80,119	
Reserve for excess and obsolete inventory	(4,207	)	(4,205	)
Inventories, net	$143,417		$ 129,879	

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Reserve for Excess and Obsolete Inventory
Changes in the reserve for excess and obsolete inventory were as follows:

(In thousands)	Six Months Ended June 30, 2017	2016
Balance at beginning of period	$4,205	$3,045
Additions charged to costs and expenses [1]	1,218	1,486
Sell through [2]	(576)	(537)
(Write-offs)/Foreign exchange effects	(640)	(445)
Balance at end of period	$4,207	$3,549

(1) The additions charged to costs and expenses do not include inventory directly written-off that was scrapped during production totaling $0.2 million and $0.2 million for the six months ended June 30, 2017 and 2016, respectively. These amounts are production waste and are not included in management's reserve for excess and obsolete inventory.
(2) These amounts represent the reduction in reserves associated with inventory items that were sold during the period.

Significant Supplier
We purchase integrated circuits, components and finished goods from multiple sources. Purchases from the following supplier totaled more than 10% of our total inventory purchases:

	Three Months Ended June 30, 2017		2016	
	$ (thousands)	% of Total Inventory Purchases	$ (thousands)	% of Total Inventory Purchases
Texas Instruments	$11,450	11.0 %	$11,437	11.8 %

	Six Months Ended June 30, 2017		2016	
	$ (thousands)	% of Total Inventory Purchases	$ (thousands)	% of Total Inventory Purchases
Texas Instruments	$20,578	10.7 %	$19,941	11.3 %

Related Party Supplier

We purchase certain printed circuit board assemblies from a related party supplier. The supplier is considered a related party for financial reporting purposes because our Senior Vice President of Strategic Operations owns 40% of this vendor. Inventory purchases from this supplier were as follows:

	Three Months Ended June 30,			
	2017		2016	
	$ (thousands)	% of Total Inventory Purchases	$ (thousands)	% of Total Inventory Purchases
Related party supplier	$1,638	1.6 %	$1,977	2.0 %

	Six Months Ended June 30,			
	2017		2016	
	$ (thousands)	% of Total Inventory Purchases	$ (thousands)	% of Total Inventory Purchases
Related party supplier	$2,584	1.3 %	$3,589	2.0 %

Total accounts payable to this supplier were as follows:

	June 30, 2017		December 31, 2016	
	$ (thousands)	% of Accounts Payable	$ (thousands)	% of Accounts Payable
Related party supplier	$1,838	1.7 %	$1,690	1.7 %

Our payment terms and pricing with this supplier are consistent with the terms offered by other suppliers in the ordinary course of business. The accounting policies that we apply to our transactions with our related party supplier are consistent with those applied in transactions with independent third parties. Corporate management routinely monitors purchases from our related party supplier to ensure these purchases remain consistent with our business objectives.

Note 5 — Goodwill and Intangible Assets, Net

Goodwill

Changes in the carrying amount of goodwill were as follows:

(In thousands)	
Balance at December 31, 2016	$43,052
Goodwill acquired during the period [1]	5,294
Foreign exchange effects	26
Balance at June 30, 2017	$48,372

[1] During the second quarter of 2017, we recorded $5.3 million of goodwill related to the Residential Control Systems, Inc. acquisition. Refer to Note 18 for further information about this acquisition.

Intangible Assets, Net

The components of intangible assets, net were as follows:

	June 30, 2017			December 31, 2016		
(In thousands)	Gross [1]	Accumulated Amortization [1]	Net	Gross [1]	Accumulated Amortization [1]	Net
Distribution rights	$329	$ (143)	$186	$302	$ (119)	$183
Patents	12,330	(4,932)	7,398	12,038	(4,775)	7,263
Trademarks and trade names [2]	2,787	(1,442)	1,345	2,400	(1,310)	1,090
Developed and core technology	12,563	(5,065)	7,498	12,585	(4,068)	8,517
Capitalized software development costs	142	(42)	100	142	(5)	137
Customer relationships [2]	32,751	(17,772)	14,979	27,703	(16,344)	11,359
Order backlog [2]	150	(37)	113	—	—	—
Total intangible assets, net	$61,052	$ (29,433)	$31,619	$55,170	$ (26,621)	$28,549

(1) This table excludes the gross value of fully amortized intangible assets totaling $5.7 million and $10.2 million at June 30, 2017 and December 31, 2016, respectively.

(2) During the second quarter of 2017, we purchased a trade name valued at $0.4 million, which is being amortized ratably over eight years; customer relationships valued at $5.2 million, which are being amortized ratably over 10 years; and order backlog valued at $0.2 million, which is being amortized ratably over one year. Refer to Note 18 for further information regarding the purchase of these intangible assets.

Amortization expense is recorded in selling, general and administrative expenses, except amortization expense related to capitalized software development costs and order backlog, which are recorded in cost of sales. Amortization expense by income statement caption was as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(In thousands)	2017	2016	2017	2016
Cost of sales	$55	$21	$74	$42
Selling, general and administrative expenses	1,736	1,534	3,317	3,067
Total amortization expense	$1,791	$1,555	$3,391	$3,109

Estimated future annual amortization expense related to our intangible assets at June 30, 2017, is as follows:

(In thousands)	
2017 (remaining 6 months)	$3,582
2018	7,152
2019	7,067
2020	5,980
2021	2,575
Thereafter	5,263
Total	$31,619

Note 6 — Line of Credit

Our Amended and Restated Credit Agreement ("Amended Credit Agreement") with U.S. Bank National Association ("U.S. Bank") provides for a $125.0 million revolving line of credit ("Credit Line") that expires on November 1, 2019 and that may be used for working capital and other general corporate purposes including acquisitions, share repurchases and capital expenditures. Amounts available for borrowing under the Credit Line are reduced by the balance of any outstanding letters of credit. There were no outstanding letters of credit at June 30, 2017.

All obligations under the Credit Line are secured by substantially all of our U.S. personal property and tangible and intangible assets as well as 65% of our ownership interest in Enson Assets Limited, our wholly-owned subsidiary that controls our manufacturing factories in the PRC.

Under the Amended Credit Agreement, we may elect to pay interest on the Credit Line based on LIBOR plus an applicable margin (varying from 1.25% to 1.75%) or base rate (based on the prime rate of U.S. Bank or as otherwise specified in the Amended Credit Agreement) plus an applicable margin (varying from 0.00% to 0.50%). The applicable margins are calculated quarterly and vary based on our cash flow leverage ratio as set forth in the Amended Credit Agreement. The interest rate in effect at June 30, 2017 was 2.34%. There are no commitment fees or unused line fees under the Amended Credit Agreement.

The Amended Credit Agreement includes financial covenants requiring a minimum fixed charge coverage ratio and a maximum cash flow leverage ratio. In addition, the Amended Credit Agreement also contains other customary affirmative and negative covenants and events of default. As of June 30, 2017, we were in compliance with the covenants and conditions of the Amended Credit Agreement.

At June 30, 2017, we had $92.0 million outstanding under the Credit Line. Our total interest expense on borrowings was $0.6 million and $0.3 million during the three months ended June 30, 2017 and 2016, respectively. Our total interest expense on borrowings was $1.1 million and $0.6 million during the six months ended June 30, 2017 and 2016, respectively.

Note 7 — Income Taxes

We utilize our estimated annual effective tax rate to determine our provision for income taxes for interim periods. The income tax provision is computed by taking the estimated annual effective tax rate and multiplying it by the year-to-date pre-tax book income.

We recorded income tax expense of $1.4 million and $1.8 million for the three months ended June 30, 2017 and 2016, respectively. Our effective tax rate was 23.2% and 21.3% during the three months ended June 30, 2017 and 2016, respectively. The increase in the effective tax rate was primarily due to the non-deductibility of certain transactions in China as a result of the pending sale of our Guangzhou factory (Note 10).

We recorded income tax expense of $1.1 million and $2.5 million for the six months ended June 30, 2017 and 2016, respectively. Our effective tax rate was 18.9% and 21.3% during the six months ended June 30, 2017 and 2016, respectively. The decrease in our effective tax rate was primarily due to the recognition of $0.4 million of excess tax benefits related to stock-based compensation during the six months ended June 30, 2017 as a result of implementing ASU 2016-09.

At June 30, 2017, we had gross unrecognized tax benefits of $3.8 million, including interest and penalties, of which $3.5 million would affect the annual effective tax rate if these tax benefits are realized. Further, we are unaware of any positions for which it is reasonably possible that the total amount of unrecognized tax benefits will significantly change within the next twelve months. However, based on federal, state and foreign statute expirations in various jurisdictions, we anticipate a decrease in unrecognized tax benefits of approximately $0.1 million within the next twelve months. We have classified uncertain tax positions as non-current income tax liabilities unless expected to be paid within one year.

We have elected to classify interest and penalties as a component of tax expense. Accrued interest and penalties of $0.3 million and $0.3 million at June 30, 2017 and December 31, 2016, respectively, are included in our unrecognized tax benefits.

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Note 8 — Accrued Compensation
The components of accrued compensation were as follows:

(In thousands)	June 30, 2017	December 31, 2016
Accrued social insurance (1)	$17,188	$ 19,974
Accrued salary/wages	8,656	7,903
Accrued vacation/holiday	2,778	2,411
Accrued bonus (2)	1,782	2,421
Accrued commission	682	933
Accrued medical insurance claims	286	122
Other accrued compensation	2,148	1,816
Total accrued compensation	$33,520	$ 35,580

(1) Effective January 1, 2008, the Chinese Labor Contract Law was enacted in the PRC. This law mandated that PRC employers remit the applicable social insurance payments to their local government. Social insurance is comprised of various components such as pension, medical insurance, job injury insurance, unemployment insurance, and a housing assistance fund, and is administered in a manner similar to social security in the United States. This amount represents our estimate of the amounts due to the PRC government for social insurance on June 30, 2017 and December 31, 2016.

(2) Accrued bonus includes an accrual for an extra month of salary ("13th month salary") to be paid to employees in certain geographies where it is the customary business practice. This 13th month salary is paid to these employees if they remain employed with us through December 31st. The total accrued for the 13th month salary was $0.6 million and $0.7 million at June 30, 2017 and December 31, 2016, respectively.

Note 9 — Other Accrued Expenses
The components of other accrued expenses were as follows:

(In thousands)	June 30, 2017	December 31, 2016
Advertising and marketing	$280	$ 213
Deferred revenue	1,444	1,431
Duties	1,047	1,127
Freight and handling fees	1,935	1,919
Product development	502	454
Product warranty claim costs	298	134
Professional fees	1,320	1,313
Property, plant, and equipment	738	1,017
Sales taxes and VAT	2,914	2,715
Short-term contingent consideration	2,500	—
Third-party commissions	667	853
Tooling (1)	1,605	1,520
Unrealized loss on foreign currency exchange contracts	667	1,623
URC court order and settlement agreement (Note 2)	—	6,622
Utilities	409	331
Other	3,968	3,138
Total other accrued expenses	$20,294	$ 24,410

(1) The tooling accrual balance relates to unearned revenue for tooling that will be sold to customers.

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Note 10 — Commitments and Contingencies
Product Warranties
Changes in the liability for product warranty claim costs were as follows:

(In thousands)	Six Months Ended June 30,	
	2017	2016
Balance at beginning of period	$134	$ 35
Accruals for warranties issued during the period	167	—
Settlements (in cash or in kind) during the period	(3)	—
Balance at end of period	$298	$ 35

Restructuring Activities and Sale of Guangzhou Factory
In the first quarter of 2016, we implemented a plan to reduce the impact of rising labor rates in China by transitioning manufacturing activities from our southern-most China factory, located in the city of Guangzhou in the Guangdong province, to our other three China factories where labor rates are rising at a slower rate. As a result, we incurred severance costs of $5.7 million and $1.5 million during the six months ended June 30, 2017 and 2016, respectively, which are included within operating expenses. We expect to incur additional severance costs of approximately $1.5 million as we continue to execute this transition over the next three to six months. Because severance costs relate to involuntary terminations, we record the related liability at the communication date. At June 30, 2017, we had $0.2 million of unpaid severance costs included within accrued compensation.
On September 26, 2016, we entered into an agreement to sell our Guangzhou manufacturing facility for RMB 320 million (approximately $47.2 million based on June 30, 2017 exchange rates). Under the terms of this agreement, we have up to 24 months to cease all operations within the facility. The closing of the sale will be subject to customary due diligence and local regulatory approval and per the terms of the agreement could take up to approximately 28 months from the execution of the agreement. In accordance with the terms of the agreement, the buyer deposited 10% of the purchase price into an escrow account at agreement inception, which we have presented as long-term restricted cash in our consolidated balance sheet (also refer to Note 2). The remaining balance of the purchase price is to be placed into the escrow account prior to the closing of the sale and will be released to us upon closing.
Litigation
On or about June 10, 2015, FM Marketing GmbH ("FMH") and Ruwido Austria GmbH ("Ruwido"), filed a Summons in Summary Proceedings in Belgium court against one of our subsidiaries, Universal Electronics BV ("UEBV") and one of its customers, Telenet N.V. ("Telenet"), claiming that one of the products UEBV supplies Telenet violates two design patents and one utility patent owned by FMH and/or Ruwido. By this summons, FMH and Ruwido sought to enjoin Telenet and UEBV from continued distribution and use of the products at issue. After the September 29, 2015 hearing, the court issued its ruling in our and Telenet's favor, rejecting FMH and Ruwido's request entirely. On October 22, 2015, Ruwido filed its notice of appeal in this ruling. The parties have fully briefed and argued before the appellate court and we are awaiting the appellate court's ruling. In addition, on or about February 9, 2016, Ruwido filed a writ of summons for proceeding on the merits with respect to asserted patents. UEBV and Telenet have replied, denying all of Ruwido's allegations and in June 2017, a hearing was held before the trial court. We are awaiting the ruling from the trial court. Finally, in September 2015, UEBV filed an Opposition with the European Patent Office seeking to invalidate the one utility patent asserted against UEBV and Telenet by Ruwido. The hearing on this opposition was held in July 2017. During this hearing the panel requested additional information. We are in the process of assembling this additional information and scheduling a date for rehearing.

On January 26, 2017, OpenTV, Inc., Nagra USA, Inc., Nagravision SA, and Kudelski SA (collectively, the "Kudelski Group") filed a request with the U.S. International Trade Commission ("ITC") to institute an investigation pursuant to Section 337 of the Tariff Act of 1930, as amended, concerning certain remote control devices we supply Comcast Corporation ("Comcast") to which the ITC agreed to accept this request. On July 21, 2017, the Kudelski Group filed a motion to terminate the investigation as to all parties, including us. We expect this motion to be accepted soon by the ITC.

There are no other material pending legal proceedings to which we or any of our subsidiaries is a party or of which our respective property is the subject. However, as is typical in our industry and to the nature and kind of business in which we are engaged, from time to time, various claims, charges and litigation are asserted or commenced by third parties against us or by us against third parties arising from or related to product liability, infringement of patent or other intellectual property rights, breach of warranty, contractual relations, or employee relations. The amounts claimed may be substantial but may not bear any reasonable relationship to the merits of the claims or the extent of any real risk of court awards assessed against us or in our favor. However, no assurances can be made as to the outcome of any of these matters, nor can we estimate the range of potential losses to us. In our opinion, final judgments, if any, which might be rendered against us in potential or pending litigation would not have a material adverse effect on our financial condition, results of operations, or cash flows. Moreover, we believe that our products do not infringe any third parties' patents or other intellectual property rights.

We maintain directors' and officers' liability insurance which insures our individual directors and officers against certain claims, as well as attorney's fees and related expenses incurred in connection with the defense of such claims.

Note 11 — Treasury Stock

From time to time, our Board of Directors authorizes management to repurchase shares of our issued and outstanding common stock on the open market. Repurchases may be made to manage dilution created by shares issued under our stock incentive plans or whenever we deem a repurchase is a good use of our cash and the price to be paid is at or below a threshold approved by our Board. As of June 30, 2017, we had 148,853 shares available for repurchase on the open market under the Board's authorizations. On July 26, 2017, our Board increased these repurchase authorizations by 51,147 shares bringing the total authorization as of the approval date to 200,000 shares. Shares may also be tendered by employees to satisfy tax withholding obligations in connection with the vesting of restricted stock.

Repurchased shares of our common stock were as follows:

	Six Months Ended June 30,	
(In thousands)	2017	2016
Shares repurchased	239	36
Cost of shares repurchased	$14,885	$1,944

Repurchased shares are recorded as shares held in treasury at cost. We hold these shares for future use as management and the Board of Directors deem appropriate, which has included compensating our outside directors.

Note 12 — Business Segment and Foreign Operations

Reportable Segment

An operating segment, in part, is a component of an enterprise whose operating results are regularly reviewed by the chief operating decision maker to make decisions about resources to be allocated to the segment and assess its performance. Operating segments may be aggregated only to a limited extent. Our chief operating decision maker, the Chief Executive Officer, reviews financial information presented on a consolidated basis, accompanied by disaggregated information about revenues for purposes of making operating decisions and assessing financial performance. Accordingly, we only have a single operating and reportable segment.

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Foreign Operations
Our net sales to external customers by geographic area were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(In thousands)	2017	2016	2017	2016
United States	$85,569	$90,872	$167,497	$174,810
Asia (excluding PRC)	26,916	20,618	51,566	42,191
People's Republic of China	21,835	23,153	37,578	40,079
Europe	19,740	18,544	37,164	34,327
Latin America	15,381	11,686	31,026	19,241
Other	8,139	6,113	14,155	10,996
Total net sales	$177,580	$170,986	$338,986	$321,644

Specific identification of the customer billing location was the basis used for attributing revenues from external customers to geographic areas.
Long-lived tangible assets by geographic area were as follows:

(In thousands)	June 30, 2017	December 31, 2016
United States	$13,004	$ 11,948
People's Republic of China	100,300	94,113
All other countries	3,969	4,186
Total long-lived tangible assets	$117,273	$ 110,247

Note 13 — Stock-Based Compensation
Stock-based compensation expense for each employee and director is presented in the same income statement caption as their cash compensation. Stock-based compensation expense by income statement caption and the related income tax benefit were as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(In thousands)	2017	2016	2017	2016
Cost of sales	$19	$15	$34	$29
Research and development expenses	144	137	263	273
Selling, general and administrative expenses:				
Employees	1,975	1,731	3,719	3,576
Outside directors	794	594	1,539	1,092
Total employee and director stock-based compensation expense	$2,932	$2,477	$5,555	$4,970
Income tax benefit	$889	$736	1,704	1,469

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Stock Options

Stock option activity was as follows:

	Number of Options (in 000's)	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in 000's)
Outstanding at December 31, 2016	652	$ 39.27		
Granted	92	62.70		
Exercised	(35)	24.41		$ 1,555
Forfeited/canceled/expired	(18)	28.08		
Outstanding at June 30, 2017 (1)	691	$ 43.41	4.88	$ 16,207
Vested and expected to vest at June 30, 2017 (1)	691	$ 43.41	4.88	$ 16,204
Exercisable at June 30, 2017 (1)	424	$ 35.97	4.25	$ 13,092

(1) The aggregate intrinsic value represents the total pre-tax value (the difference between our closing stock price on the last trading day of the second quarter of 2017 and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders had they all exercised their options on June 30, 2017. This amount will change based on the fair market value of our stock.

The assumptions we utilized in the Black-Scholes option pricing model and the resulting weighted average fair value of stock option grants were the following:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Weighted average fair value of grants	$—	$ —	$ 19.61	$ 17.96
Risk-free interest rate	—%	—%	1.75 %	1.36 %
Expected volatility	—%	—%	34.25 %	41.38 %
Expected life in years	0.00	0.00	4.52	4.55

As of June 30, 2017, we expect to recognize $4.3 million of total unrecognized pre-tax stock-based compensation expense related to non-vested stock options over a remaining weighted-average life of 1.9 years.

Restricted Stock

Non-vested restricted stock award activity was as follows:

	Shares (in 000's)	Weighted-Average Grant Date Fair Value
Non-vested at December 31, 2016	153	$ 57.43
Granted	99	63.40
Vested	(43)	59.64
Forfeited	(4)	60.64
Non-vested at June 30, 2017	205	$ 59.78

As of June 30, 2017, we expect to recognize $9.6 million of total unrecognized pre-tax stock-based compensation expense related to non-vested restricted stock awards over a weighted-average life of 2.0 years.

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Note 14 — Performance-Based Common Stock Warrants
On March 9, 2016, we issued common stock purchase warrants to Comcast to purchase up to 725,000 shares of our common stock at a price of $54.55 per share. The right to exercise the warrants is subject to vesting over three successive two-year periods (with the first two-year period commencing on January 1, 2016) based on the level of purchases of goods and services from us by Comcast and its affiliates, as defined in the warrants. The table below presents the purchase levels and number of warrants that will vest in each period based upon achieving these purchase levels.

Aggregate Level of Purchases by Comcast and Affiliates	Incremental Warrants That Will Vest January 1, 2016 - December 31, 2017	January 1, 2018 - December 31, 2019	January 1, 2020 - December 31, 2021
$260 million	100,000	100,000	75,000
$300 million	75,000	75,000	75,000
$340 million	75,000	75,000	75,000
Maximum Potential Warrants Earned by Comcast	250,000	250,000	225,000

If total aggregate purchases by Comcast and its affiliates are below $260 million in any of the two-year periods above, no warrants will vest related to that two-year period. If total aggregate purchases of goods and services by Comcast and its affiliates exceed $340 million during either the first or second two-year period, the amount of any such excess will count toward aggregate purchases in the following two-year period. To fully vest in the rights to purchase all of the underlying shares, Comcast and its affiliates must purchase an aggregate of $1.02 billion in goods and services from us during the six-year vesting period.
Any and all warrants that vest will expire on January 1, 2023. The warrants provide for certain adjustments that may be made to the exercise price and the number of shares issuable upon exercise due to customary anti-dilution provisions. Additionally, in connection with the warrants, we have also entered into a registration rights agreement with Comcast under which Comcast may from time to time request that we register the shares of common stock underlying vested warrants with the SEC.
Because the warrants contain performance criteria under which Comcast must achieve specified aggregate purchase levels for the warrants to vest, as detailed above, the measurement date for the warrants is the date on which the warrants vest. At June 30, 2017, none of the warrants had vested.
The fair value of the warrants is determined using the Black-Scholes option pricing model. The assumptions we utilized and the resulting fair value of the warrants were the following:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Fair value	$28.89	$35.88	$28.89	$35.88
Price of Universal Electronics Inc. common stock	$67.21	$71.16	$67.21	$71.16
Risk-free interest rate	1.95 %	1.22 %	1.95 %	1.22 %
Expected volatility	35.05 %	41.17 %	35.05 %	41.17 %
Expected life in years	5.50	6.50	5.50	6.50

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The impact to net sales recorded in connection with the warrants and the related income tax benefit were as follows:

	Three months ended June 30,		Six months ended June 30,	
(in thousands)	2017	2016	2017	2016
Reduction to net sales	$331	$1,193	$1,263	$2,059
Income tax benefit	123	438	471	756

At June 30, 2017, we estimated the number of warrants that will vest based on the combination of purchases already made and projected future purchases that will be made by Comcast and its affiliates. These estimates may increase or decrease based on actual future purchases. The aggregate unrecognized estimated fair value of unvested warrants at June 30, 2017 was $17.0 million.

Note 15 — Other Income (Expense), Net

Other income (expense), net consisted of the following:

	Three Months Ended June 30,		Six Months Ended June 30,	
(In thousands)	2017	2016	2017	2016
Net gain (loss) on foreign currency exchange contracts [1]	$(1,598)	$(477)	$(1,364)	$(676)
Net gain (loss) on foreign currency exchange transactions	1,006	1,105	1,336	2,016
Other income (expense)	(50)	43	(31)	51
Other income (expense), net	$(642)	$671	$(59)	$1,391

[1] This represents the gains (losses) incurred on foreign currency hedging derivatives (see Note 17 for further details).

Note 16 — Earnings Per Share

Earnings per share was calculated as follows:

	Three Months Ended June 30,		Six Months Ended June 30,	
(In thousands, except per-share amounts)	2017	2016	2017	2016
BASIC				
Net income attributable to Universal Electronics Inc.	$4,684	$6,590	$4,803	$9,311
Weighted-average common shares outstanding	14,404	14,440	14,427	14,406
Basic earnings per share attributable to Universal Electronics Inc.	$0.33	$0.46	$0.33	$0.65
DILUTED				
Net income attributable to Universal Electronics Inc.	$4,684	$6,590	$4,803	$9,311
Weighted-average common shares outstanding for basic	14,404	14,440	14,427	14,406
Dilutive effect of stock options and restricted stock	279	295	273	280
Weighted-average common shares outstanding on a diluted basis	14,683	14,735	14,700	14,686
Diluted earnings per share attributable to Universal Electronics Inc.	$0.32	$0.45	$0.33	$0.63

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The number of stock options and shares of restricted stock excluded from the computation of diluted earnings per common share were as follows:

(In thousands)	Three Months Ended June 30, 2017	2016	Six Months Ended June 30, 2017	2016
Stock options	165	78	147	167
Restricted stock awards	—	1	29	10

Note 17 — Derivatives

The following table sets forth the total net fair value of derivatives:

(In thousands)	June 30, 2017 Fair Value Measurement Using Level 1	Level 2	Level 3	Total Balance	December 31, 2016 Fair Value Measurement Using Level 1	Level 2	Level 3	Total Balance
Foreign currency exchange contracts	$ —	$ (479)	$ —	$ (479)	$ —	$ (1,584)	$ —	$ (1,584)

We held foreign currency exchange contracts, which resulted in a net pre-tax loss of $1.6 million and $0.5 million for the three months ended June 30, 2017 and 2016, respectively. For the six months ended June 30, 2017 and 2016, we had a net pre-tax loss of $1.4 million and $0.7 million, respectively (see Note 15).

Details of foreign currency exchange contracts held were as follows:

Date Held	Type	Position Held	Notional Value (in millions)	Forward Rate	Unrealized Gain/(Loss) Recorded at Balance Sheet Date (in thousands)[(1)]	Settlement Date
June 30, 2017	USD/Euro	USD	$ 21.0	1.1149	$ (537)	July 28, 2017
June 30, 2017	USD/Chinese Yuan Renminbi	USD	$ 12.0	6.8655	$ (128)	July 28, 2017
June 30, 2017	USD/Brazilian Real	USD	$ 4.5	3.2330	$ 188	October 20, 2017
June 30, 2017	USD/Brazilian Real	BRL	$ 1.0	3.3660	$ (2)	October 20, 2017
December 31, 2016	USD/Euro	USD	$ 18.0	1.0513	$ (61)	January 27, 2017
December 31, 2016	USD/Chinese Yuan Renminbi	Chinese Yuan Renminbi	$ 25.0	6.7230	$ (974)	January 13, 2017
December 31, 2016	USD/Chinese Yuan Renminbi	Chinese Yuan Renminbi	$ 10.0	6.6757	$ (457)	January 13, 2017

December 31, 2016	USD/Brazilian Real	USD	$ 2.0	3.4775	$ (131)	January 13, 2017
December 31, 2016	USD/Brazilian Real	USD	$ 4.0	3.2316	$ 39	January 13, 2017

(1) Unrealized gains on foreign currency exchange contracts are recorded in prepaid expenses and other current assets. Unrealized losses on foreign currency exchange contracts are recorded in other accrued expenses.

Note 18 — Business Combination

On April 6, 2017, we acquired substantially all of the net assets of Residential Control Systems, Inc. ("RCS"), a U.S.-based designer and manufacturer of energy management and control products for the residential, small commercial and hospitality markets. The initial purchase price of $12.6 million was comprised of $8.9 million in cash, which is subject to adjustment based on the final acquired working capital balances, and $3.7 million of contingent consideration. Additionally, we incurred approximately $0.1 million in acquisition costs, consisting primarily of accounting related expenses, which are included within selling, general and administrative expenses for the three and six months ended June 30, 2017. The acquisition of these assets will allow us to expand our product offering of home sensing, monitoring and control solutions to include smart thermostat, sensing and monitoring products currently sold and marketed by RCS.

Our consolidated income statement for the three and six months ended June 30, 2017 includes net sales of $1.4 million and a net loss of $0.4 million attributable to RCS for the period commencing on April 6, 2017.

Contingent Consideration

The initial purchase price is subject to adjustment for differences between the initial estimated working capital balances and the final adjusted balances. In accordance with the terms of the RCS Asset Purchase Agreement ("APA"), any adjustment to the initial purchase price must be completed within 120 days of the acquisition date. We expect this calculation to be completed in the third quarter of 2017.

We are required to make additional earnout payments of up to $10.0 million upon the achievement of certain operating income levels attributable to RCS over the period commencing on the acquisition date through June 30, 2022. The amount of contingent consideration is calculated at the end of each calendar year and is based upon the agreed upon percentage of operating income as defined in the APA. Operating income will be calculated using certain revenues, costs and expenses directly attributable to RCS as specified in the APA. At the acquisition date, the value of earnout contingent consideration was estimated using a valuation methodology based on projections of future operating income calculated in accordance with the APA. Such projections were then discounted using an average discount rate of 24.8% to reflect the risk in achieving the projected operating income levels as well as the time value of money. The fair value measurement of the earnout contingent consideration was based primarily on significant inputs not observable in an active market and thus represents a Level 3 measurement as defined under U.S. GAAP. The fair value of earnout consideration is presented as long-term contingent consideration in our consolidated balance sheet at June 30, 2017.

Preliminary Purchase Price Allocation

Using the acquisition method of accounting, the acquisition date fair value of the consideration transferred was allocated to the net tangible and intangible assets acquired and liabilities assumed based on their estimated fair values on the acquisition date. The excess of the purchase price over the estimated fair value of net assets acquired is recorded as goodwill. The goodwill is expected to be deductible for income tax purposes. Management's preliminary purchase price allocation as of June 30, 2017 was the following:

(in thousands)	Estimated Lives	Preliminary Fair Value
Accounts receivable		$ 429
Inventories		1,460
Prepaid expenses and other current assets		6
Property, plant and equipment	1-4 years	14
Current liabilities		(399)
Net tangible assets acquired		1,510
Trade name	8 years	400

Customer relationships	10 years	5,200
Order backlog	1 year	150
Goodwill		5,294
Total purchase price		12,554
Less: Contingent consideration		(3,700)
Cash paid		$ 8,854

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Management's determination of the fair value of intangible assets acquired are based primarily on significant inputs not observable in an active market and thus represent Level 3 fair value measurements as defined under U.S. GAAP. The fair value assigned to the RCS trade name intangible asset was determined utilizing a relief from royalty method. Under the relief from royalty method, the fair value of the intangible asset is estimated to be the present value of the royalties saved because the company owns the intangible asset. Revenue projections and estimated useful life were significant inputs into estimating the value of the RCS trade name.

The fair value assigned to RCS customer relationships and order backlog intangible assets were determined utilizing a multi-period excess earnings approach. Under the multi-period excess earnings approach, the fair value of the intangible asset is estimated to be the present value of future earnings attributable to the asset and utilizes revenue and cost projections, including an assumed contributory asset charge.

The trade name, customer relationships, and order backlog intangible assets are expected to be deductible for income tax purposes.

Pro Forma Results (Unaudited)

The following unaudited pro forma financial information presents the combined results of our operations and the operations of RCS as if this transaction had occurred on January 1, 2016. This unaudited pro forma financial information is not intended to represent or be indicative of the consolidated results of operations that would have been achieved had the acquisition actually been completed as of January 1, 2016, and should not be taken as a projection of the future consolidated results of our operations.

	Three Months Ended June 30, 2017		Six Months Ended June 30, 2017	
(In thousands, except per-share amounts)	2017	2016	2017	2016
Net sales	$177,580	$172,308	$339,548	$326,514
Net income	4,767	6,381	4,541	9,367
Net income attributable to Universal Electronics Inc.	4,767	6,373	4,541	9,337
Basic earnings per share attributable to Universal Electronics Inc.	$0.33	$0.44	$0.31	$0.65
Diluted earnings per share attributable to Universal Electronics Inc.	$0.32	$0.43	$0.31	$0.64

For purposes of determining pro forma net income attributable to Universal Electronics Inc., adjustments were made to all periods presented in the table above. The pro forma net income and net income attributable to Universal Electronics Inc. assumes that amortization of acquired intangible assets began at January 1, 2016 rather than on April 6, 2017. The result is a net increase in amortization expense of $0.1 million for the six months ended June 30, 2017 and a net increase in amortization expense of $0.2 million and $0.4 million for the three and six months ended June 30, 2016, respectively. Additionally, acquisition costs totaling $0.1 million are excluded from pro forma net income attributable to Universal Electronics Inc. All adjustments have been made net of their related tax effects.

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

The following discussion should be read in conjunction with the Consolidated Financial Statements and the related notes that appear elsewhere in this document.

Overview

We develop and manufacture a broad line of pre-programmed universal remote control products, AV accessories, software and intelligent wireless security, sensing and automation components dedicated to redefining the home entertainment and automation experience. Our customers operate primarily in the consumer electronics market and include subscription broadcasters, OEMs, international retailers, private label brands, pro-security dealers and companies in the computing industry. We also sell integrated circuits, on which our software and device control database is embedded, and license our device control database to OEMs that manufacture televisions, digital audio and video players, streamer boxes, cable converters, satellite receivers, set-top boxes, room air conditioning equipment, game consoles, and wireless mobile phones and tablets.

Since our beginning in 1986, we have compiled an extensive device control code database that covers approximately one million individual device functions and approximately 8,000 unique consumer electronic brands. QuickSet®, our proprietary software, can automatically detect, identify and enable the appropriate control commands for home entertainment, automation and appliances like air conditioners. Our library is regularly updated with new control functions captured directly from devices, remote controls and manufacturer specifications to ensure the accuracy and integrity of our database and control engine. Our universal remote control library contains device codes that are capable of controlling virtually all set-top boxes, televisions, audio components, DVD players, Blu-Ray players, and CD players, as well as most other remote controlled home entertainment devices and home automation control modules worldwide.

With the wider adoption of more advanced technologies, emerging radio frequency ("RF") technologies, such as RF4CE, Bluetooth, and Bluetooth Smart, have increasingly become a focus in our development efforts. Several new recently released platforms utilize RF to effectively implement popular features like voice search.

We have developed a comprehensive patent portfolio of more than 400 pending and issued patents related to remote controls and home automation.

We operate as one business segment. We have 24 international subsidiaries located in Argentina, Brazil, British Virgin Islands, Cayman Islands, France, Germany, Hong Kong (3), India, Italy, Japan, Korea, Mexico, the Netherlands, People's Republic of China (6), Singapore, Spain, and the United Kingdom.

To recap our results for the three months ended June 30, 2017:

- Net sales increased 3.9% to $177.6 million for the three months ended June 30, 2017 from $171.0 million for the three months ended June 30, 2016.
- Our gross margin percentage decreased from 25.4% for the three months ended June 30, 2016 to 24.6% for the three months ended June 30, 2017.
- Operating expenses, as a percent of net sales, decreased from 20.7% for the three months ended June 30, 2016 to 20.5% for the three months ended June 30, 2017.
- Our operating income decreased from $8.0 million for the three months ended June 30, 2016 to $7.3 million for the three months ended June 30, 2017, and our operating margin percentage decreased from 4.7% for the three months ended June 30, 2016 to 4.1% for the three months ended June 30, 2017.
- Our effective tax rate increased to 23.2% for the three months ended June 30, 2017, compared to 21.3% for the three months ended June 30, 2016.

Our strategic business objectives for 2017 include the following:

- continue to develop and market the advanced remote control products and technologies our customer base is adopting;
- continue to broaden our home control and automation product offerings;
- further penetrate international subscription broadcasting markets;
- acquire new customers in historically strong regions;
- increase our share with existing customers; and
- continue to seek acquisitions or strategic partners that complement and strengthen our existing business.

We intend for the following discussion of our financial condition and results of operations to provide information that will assist in understanding our consolidated financial statements, the changes in certain key items in those financial statements from period

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to period, and the primary factors that accounted for those changes, as well as how certain accounting principles, policies and estimates affect our consolidated financial statements.

Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with accounting principles accepted in the United States of America requires us to make estimates and judgments that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. On an on-going basis, we evaluate our estimates and judgments, including those related to revenue recognition, allowances for sales returns and doubtful accounts, inventory valuation, our review for impairment of long-lived assets, intangible assets and goodwill, business combinations, income taxes, stock-based compensation expense and performance-based common stock warrants. Actual results may differ from these judgments and estimates, and they may be adjusted as more information becomes available. Any adjustment may be significant and may have a material impact on our consolidated financial position or results of operations.

An accounting policy is deemed to be critical if it requires an accounting estimate to be made based on assumptions about matters that are highly uncertain at the time the estimate is made, if different estimates reasonably may have been used, or if changes in the estimate that are reasonably likely to occur may materially impact the financial statements. We do not believe that there have been any significant changes during the three months ended June 30, 2017 to the items that we disclosed as our critical accounting policies and estimates in Item 7, "Management's Discussion and Analysis of Financial Condition and Results of Operations" contained in our Annual Report on Form 10-K for our fiscal year ended December 31, 2016.

Recent Accounting Pronouncements

See Note 1 contained in the "Notes to Consolidated Financial Statements" for a discussion of recent accounting pronouncements.

Results of Operations

The following table sets forth our results of operations expressed as a percentage of net sales for the periods indicated.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2017	2016	2017	2016
Net sales	100.0 %	100.0 %	100.0 %	100.0 %
Cost of sales	75.4	74.6	75.0	74.8
Gross profit	24.6	25.4	25.0	25.2
Research and development expenses	2.8	3.0	3.1	3.2
Factory transition restructuring charges	0.2	0.0	1.7	0.5
Selling, general and administrative expenses	17.5	17.7	18.2	18.1
Operating income	4.1	4.7	2.0	3.4
Interest income (expense), net	(0.3)	(0.2)	(0.3)	(0.1)
Other income (expense), net	(0.4)	0.4	(0.0)	0.4
Income before provision for income taxes	3.4	4.9	1.7	3.7
Provision for income taxes	0.8	1.0	0.3	0.8
Net income	2.6	3.9	1.4	2.9
Net income attributable to noncontrolling interest	—	0.0	—	0.0
Net income attributable to Universal Electronics Inc.	2.6 %	3.9 %	1.4 %	2.9 %

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Three Months Ended June 30, 2017 versus Three Months Ended June 30, 2016

Net sales. Net sales for the three months ended June 30, 2017 were $177.6 million, an increase of 3.9% compared to $171.0 million for the three months ended June 30, 2016. Net sales by our Business and Consumer lines were as follows:

	Three Months Ended June 30,					
	2017			2016		
	$ (millions)	% of total		$ (millions)	% of total	
Business	$164.5	92.6	%	$158.5	92.7	%
Consumer	13.1	7.4		12.5	7.3	
Total net sales	$177.6	100.0	%	$171.0	100.0	%

Net sales in our Business lines (subscription broadcasting, OEM, and computing companies) were 92.6% of net sales for the three months ended June 30, 2017 compared to 92.7% for the three months ended June 30, 2016. Net sales in our Business lines for the three months ended June 30, 2017 increased by 3.8% to $164.5 million from $158.5 million driven primarily by the rollout of higher end platforms in North America and Europe, increased sales of home security products and increased market share in Latin America. These increases were partially offset by decreased sales to North American satellite broadcasting customers as certain customers are in the process of depleting their current stock of inventory in preparation for the launch of their new advanced platforms.

Net sales in our Consumer lines (One For All® retail and private label) were 7.4% of net sales for the three months ended June 30, 2017 compared to 7.3% for the three months ended June 30, 2016. Net sales in our Consumer lines for the three months ended June 30, 2017 increased by 4.8% to $13.1 million from $12.5 million in the three months ended June 30, 2016 driven primarily by growth in the U.S. market.

Gross profit. Gross profit for the three months ended June 30, 2017 was $43.8 million compared to $43.5 million for the three months ended June 30, 2016. Gross profit as a percent of sales decreased to 24.6% for the three months ended June 30, 2017 compared to 25.4% for the three months ended June 30, 2016. The gross margin percentage was unfavorably impacted by manufacturing inefficiencies experienced due to factory transition activities in China, price reductions granted to certain large volume customers, and lower-margin projects undertaken in Latin America. These were partially offset by the weakening of the Chinese Yuan Renminbi relative to the U.S. Dollar and improved margins in our Consumer lines.

Research and development ("R&D") expenses. R&D expenses decreased 4.0% to $4.9 million for the three months ended June 30, 2017 from $5.2 million for the three months ended June 30, 2016.

Factory transition restructuring charges. In the first quarter of 2016, we implemented a plan to reduce the impact of rising labor rates in China by transitioning manufacturing activities from our southern-most China factory, located in the city of Guangzhou in the Guangdong province, to our other three China factories where labor rates are rising at a slower rate. As a result, we incurred severance costs of $0.4 million and $0.1 million for the three months ended June 30, 2017 and 2016, respectively. We expect to incur additional severance costs of approximately $1.5 million as we continue to execute this transition over the next three to six months.

Selling, general and administrative ("SG&A") expenses. SG&A expenses increased 2.6% to $31.1 million for the three months ended June 30, 2017 from $30.3 million for the three months ended June 30, 2016. The increase was primarily due to increased payroll and benefits costs attributable to annual merit increases and additional headcount to support product development efforts; incremental expense recorded to reflect an increase in the value of contingent consideration to be paid in connection with our acquisition of the net assets of Ecolink Intelligent Technology, Inc. ("Ecolink"); additional outside product development expense; additional expense related to the acquisition of the net assets of Residential Control Systems, Inc. ("RCS"); and additional expense to support our implementation of a new ERP system. Partially offsetting these increases was a decrease in legal expense as a result of higher legal fees, including the recording of a $2.0 million legal settlement, in the prior year period related to a patent litigation lawsuit. In addition, incentive compensation expense decreased from the prior year quarter.

Interest income (expense), net. Net interest expense was $0.6 million for the three months ended June 30, 2017 compared to net interest expense of $0.3 million for the three months ended June 30, 2016 as a result of an increased level of borrowings on our line of credit.

Other income (expense), net. Net other expense was $0.6 million for the three months ended June 30, 2017 compared to net other income of $0.7 million for the three months ended June 30, 2016. This change was driven primarily by foreign currency losses associated with fluctuations in the Chinese Yuan Renminbi and Euro exchange rates versus the U.S. Dollar.

Income tax provision. Income tax expense was $1.4 million for the three months ended June 30, 2017 compared to $1.8 million for the three months ended June 30, 2016. Our effective tax rate was 23.2% for the three months ended June 30, 2017 compared to 21.3% for the three months ended June 30, 2016. The increase in our effective tax rate was primarily due to the nondeductibility of certain transactions in China as a result of the pending sale of our Guangzhou factory.

Six Months Ended June 30, 2017 versus Six Months Ended June 30, 2016

Net sales. Net sales for the six months ended June 30, 2017 were $339.0 million, an increase of 5.4% compared to $321.6 million for the six months ended June 30, 2016. Net sales by our Business and Consumer lines were as follows:

	Six Months Ended June 30,			
	2017		2016	
	$ (millions)	% of total	$ (millions)	% of total
Business	$314.9	92.9 %	$299.1	93.0 %
Consumer	24.1	7.1	22.5	7.0 %
Total net sales	$339.0	100.0 %	$321.6	100.0 %

Net sales in our Business lines (subscription broadcasting, OEM, and computing companies) were 92.9% of net sales for the six months ended June 30, 2017 compared to 93.0% for the six months ended June 30, 2016. Net sales in our Business lines for the six months ended June 30, 2017 increased by 5.3% to $314.9 million from $299.1 million driven primarily by the rollout of higher end platforms in North America and Europe, increased sales of home security products and increased market share in Latin America. These increases were partially offset by decreased sales to North American satellite customers as certain customers are in the process of depleting their current stock of inventory in preparation for the launch of their new advanced platforms.

Net sales in our Consumer lines (One For All® retail and private label) were 7.1% of net sales for the six months ended June 30, 2017 compared to 7.0% for the six months ended June 30, 2016. Net sales in our Consumer lines for the six months ended June 30, 2017 increased by 7.1% to $24.1 million from $22.5 million in the six months ended June 30, 2016 driven primarily by growth in the U.S. market.

Gross profit. Gross profit for the six months ended June 30, 2017 was $84.8 million compared to $81.1 million for the six months ended June 30, 2016. Gross profit as a percent of sales decreased slightly to 25.0% for the six months ended June 30, 2017 compared to 25.2% for the six months ended June 30, 2016. The gross margin percentage was unfavorably impacted by manufacturing inefficiencies experienced due to factory transition activities in China, price reductions granted to certain large volume customers, and lower-margin projects undertaken in Latin America. These were partially offset by the weakening of the Chinese Yuan Renminbi relative to the U.S. Dollar and improved margins in our Consumer lines.

Research and development expenses. R&D expenses increased 1.0% to $10.4 million for the six months ended June 30, 2017 from $10.3 million for the six months ended June 30, 2016.

Factory transition restructuring charges. In the first quarter of 2016, we implemented a plan to reduce the impact of rising labor costs in China by transitioning manufacturing activities from our southern-most China factory, located in the city of Guangzhou in the Guangdong province, to our other three China factories where labor rates are rising at a slower rate. As a result, we incurred severance costs of $5.7 million and $1.5 million for the six months ended June 30, 2017 and 2016, respectively. We expect to incur additional severance costs of approximately $1.5 million as we continue to execute this transition over the next three to six months.

Selling, general and administrative expenses. SG&A expenses increased 5.9% to $61.7 million for the six months ended June 30, 2017 from $58.2 million for the six months ended June 30, 2016. The increase was primarily due to incremental expense recorded to reflect an increase in the value of contingent consideration to be paid in connection with our acquisition of the net assets of Ecolink; additional expense to support our implementation of a new ERP system; additional outside product development expense; increased payroll and benefits costs attributable to annual merit increases and additional headcount to support product development efforts; and additional expense related to the acquisition of the net assets of RCS. Partially offsetting these increases was a decrease in legal expense as a result of higher legal fees, including the recording of a $2.0 million legal settlement, in the prior year period related to a patent

litigation lawsuit. In addition, incentive compensation expense decreased from the prior year period.
Interest income (expense), net. Net interest expense was $1.0 million for the six months ended June 30, 2017 compared to net interest expense of $0.5 million for the six months ended June 30, 2016 as a result of an increased level of borrowings on our line of credit.

Other income (expense), net. Net other expense was $0.1 million for the six months ended June 30, 2017 compared to net other income of $1.4 million for the six months ended June 30, 2016. This change was driven primarily by a decrease in foreign currency gains associated with fluctuations in the Chinese Yuan Renminbi exchange rate versus the U.S. Dollar.

Income tax provision. Income tax expense was $1.1 million for the six months ended June 30, 2017 compared to $2.5 million for the six months ended June 30, 2016. Our effective tax rate was 18.9% for the six months ended June 30, 2017 compared to 21.3% for the six months ended June 30, 2016. The decrease in our effective tax rate was primarily due to the recognition of $0.4 million of excess tax benefits related to stock-based compensation during the six months ended June 30, 2017 as a result of implementing ASU 2016-09, which became effective January 1, 2017.

Liquidity and Capital Resources

Sources and Uses of Cash

(In thousands)	Six Months Ended June 30, 2017	Increase (Decrease)	Six Months Ended June 30, 2016
Cash provided by (used for) operating activities	$ (249)	$ (23,500)	$ 23,251
Cash used for investing activities	(27,138)	(8,204)	(18,934)
Cash provided by (used for) financing activities	27,970	33,344	(5,374)
Effect of exchange rate changes on cash	(1,499)	965	(2,464)
Net increase (decrease) in cash and cash equivalents	$ (916)	$ 2,605	$ (3,521)

	June 30, 2017	Increase (Decrease)	December 31, 2016
Cash and cash equivalents	$ 49,695	$ (916)	$ 50,611
Working capital	87,889	(20,402)	108,291

Net cash used for operating activities was $0.2 million during the six months ended June 30, 2017 compared to $23.3 million of net cash provided by operating activities during the six months ended June 30, 2016. The decrease in net cash provided by operating activities was primarily due to working capital needs associated with inventories and accounts receivable. Cash outflows associated with inventories increased during the six months ended June 30, 2017 as a result of increased sales as well as some buildup of inventory related to the anticipated rollout of higher end platforms to certain customers. Our inventory turns decreased from 4.3 turns at June 30, 2016 to 3.9 turns at June 30, 2017. With respect to accounts receivable, cash outflows have increased primarily as a result of sales growth and collection timing. Days sales outstanding have increased from 70 days at June 30, 2016 to 75 days at June 30, 2017.

Net cash used for investing activities during the six months ended June 30, 2017 was $27.1 million compared to $18.9 million during the six months ended June 30, 2016. The increase in cash used for investing activities was driven primarily by our acquisition of the net assets of RCS for $8.9 million in April 2017. We anticipate that property, plant and equipment purchases in 2017 will total between $24 million and $27 million.

Net cash provided by financing activities was $28.0 million during the six months ended June 30, 2017 compared to $5.4 million of net cash used for financing activities during the six months ended June 30, 2016. The increase in cash provided by financing activities was driven primarily by net borrowings on our line of credit of $42.0 million during the six months ended June 30, 2017, compared to net payments of $7.0 million on our line of credit during the six months ended June 30, 2016. This was partially offset by an increase of $12.9 million in treasury stock purchases. During the six months ended June 30, 2017, we repurchased 239,470 shares of our common stock at a cost of $14.9 million compared to our repurchase of 36,329 shares at a cost of $1.9 million during the six months ended June 30, 2016. We hold these shares as treasury stock and they are available for reissue. Presently, we have no plans to distribute these shares, although we may change these plans if necessary to fulfill our on-going business objectives. From time to time, our Board of Directors authorizes management to repurchase shares of our issued and outstanding common stock on the open market. Repurchases may be made to manage dilution created by shares issued under our stock incentive plans or whenever we deem a repurchase is a good use of our cash and the price to be paid is at or below a threshold approved by our Board. As of June 30, 2017, we had 148,853 shares available for repurchase on the open market under the Board's authorizations. On July 26, 2017, our Board increased these repurchase authorizations by 51,147 shares bringing the total authorization as of the approval date to 200,000 shares.

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Contractual Obligations

The following table summarizes our contractual obligations and the effect these obligations are expected to have on our liquidity and cash flow in future periods.

	Payments Due by Period				
(In thousands)	Total	Less than 1 year	1 - 3 years	4 - 5 years	After 5 years
Operating lease obligations	$13,402	$4,591	$5,246	$3,047	$518
Capital lease obligations	3	3	—	—	—
Purchase obligations[1]	8,235	8,235	—	—	—
Contingent consideration [2]	15,100	2,500	8,222	4,194	184
Total contractual obligations	$36,740	$15,329	$13,468	$7,241	$702

(1) Purchase obligations primarily consist of contractual payments to purchase property, plant and equipment.

(2) Contingent consideration consists of contingent payments related to our purchases of the net assets of Ecolink and RCS.

Liquidity

Historically, we have utilized cash provided from operations as our primary source of liquidity, as internally generated cash flows have been sufficient to support our business operations, capital expenditures and discretionary share repurchases. More recently, we have utilized our revolving line of credit to fund an increased level of share repurchases and our acquisitions of the net assets of Ecolink and RCS. We anticipate that we will continue to utilize both cash flows from operations and our revolving line of credit to support ongoing business operations, capital expenditures and future discretionary share repurchases. Our working capital needs have typically been greatest during the third and fourth quarters when accounts receivable and inventories increase in connection with the fourth quarter holiday selling season and when inventory levels increase in anticipation of factory closures in observance of Chinese New Year. We believe our current cash balances, anticipated cash flow to be generated from operations and available borrowing resources will be sufficient to cover expected cash outlays during the next twelve months; however, because our cash is located in various jurisdictions throughout the world, we may at times need to increase borrowing from our revolving line of credit or take on additional debt until we are able to transfer cash among our various entities.

Our liquidity is subject to various risks including the risks discussed under "Item 3. Quantitative and Qualitative Disclosures about Market Risk."

(In thousands)	June 30, 2017	December 31, 2016
Cash and cash equivalents	$49,695	$ 50,611
Available borrowing resources	33,000	35,000

Our cash balances are held in numerous locations throughout the world. The majority of our cash is held outside of the United States and may be repatriated to the United States but, under current law, would be subject to United States federal income taxes, less applicable foreign tax credits. Repatriation of some foreign balances is restricted by local laws. We have not provided for the United States federal tax liability on these amounts for financial statement purposes as this cash is considered indefinitely reinvested outside of the United States. Our intent is to meet our domestic liquidity needs through ongoing cash flows, external borrowings, or both. We utilize a variety of tax planning strategies in an effort to ensure that our worldwide cash is available in the locations in which it is needed.

On June 30, 2017, we had $6.4 million, $17.2 million, $4.8 million, $17.2 million and $4.1 million of cash and cash equivalents in the United States, the People's Republic of China ("PRC"), Asia (excluding the PRC), Europe, and South America, respectively. On December 31, 2016, we had $3.3 million, $22.1 million, $5.3 million, $19.6 million, and $0.3 million of cash and cash equivalents in the United States, the PRC, Asia (excluding the PRC), Europe and South America, respectively. We attempt to mitigate our exposure to liquidity, credit and other relevant risks by placing our cash and cash equivalents with financial institutions we believe are high quality.

Our Amended and Restated Credit Agreement ("Amended Credit Agreement") with U.S. Bank National Association ("U.S. Bank") provides for a $125.0 million revolving line of credit ("Credit Line") that expires on November 1, 2019 and that may be used for working capital and other general corporate purposes including acquisitions, share repurchases and capital expenditures. Amounts available for borrowing under the Credit Line are reduced by the balance of any outstanding letters of credit. There were no outstanding letters of credit at June 30, 2017.

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All obligations under the Credit Line are secured by substantially all of our U.S. personal property and tangible and intangible assets as well as 65% of our ownership interest in Enson Assets Limited, our wholly-owned subsidiary that controls our manufacturing factories in the PRC.
Under the Amended Credit Agreement, we may elect to pay interest on the Credit Line based on LIBOR plus an applicable margin (varying from 1.25% to 1.75%) or base rate (based on the prime rate of U.S. Bank or as otherwise specified in the Amended Credit Agreement) plus an applicable margin (varying from 0.00% to 0.50%). The applicable margins are calculated quarterly and vary based on our cash flow leverage ratio as set forth in the Amended Credit Agreement. The interest rate in effect at June 30, 2017 was 2.34%. There are no commitment fees or unused line fees under the Amended Credit Agreement.
The Amended Credit Agreement includes financial covenants requiring a minimum fixed charge coverage ratio and a maximum cash flow leverage ratio. In addition, the Amended Credit Agreement also contains other customary affirmative and negative covenants and events of default. As of June 30, 2017, we were in compliance with the covenants and conditions of the Amended Credit Agreement.
At June 30, 2017, we had an outstanding balance of $92.0 million on our Credit Line and $33.0 million of availability.
Off-Balance Sheet Arrangements
We do not participate in any material off-balance sheet arrangements.

Factors That May Affect Financial Condition and Future Results

Forward-Looking Statements
We caution that the following important factors, among others (including but not limited to factors discussed in "Management's Discussion and Analysis of Financial Condition and Results of Operations," as well as those discussed in our 2016 Annual Report on Form 10-K, or in our other reports filed from time to time with the Securities and Exchange Commission), may affect our actual results and may contribute to or cause our actual consolidated results to differ materially from those expressed in any of our forward-looking statements. The factors included here are not exhaustive. Further, any forward-looking statement speaks only as of the date on which such statement is made, and we undertake no obligation to update any forward-looking statement to reflect events or circumstances after the date on which such statement is made or to reflect the occurrence of unanticipated events. New factors emerge from time to time, and it is not possible for management to predict all such factors, nor can we assess the impact of each such factor on the business or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statement. Therefore, forward-looking statements should not be relied upon as a prediction of actual future results.
While we believe that the forward-looking statements made in this report are based on reasonable assumptions, the actual outcome of such statements is subject to a number of risks and uncertainties, including the significant percentage of our revenue attributable to a limited number of customers; the failure of our markets to continue growing and expanding in the manner we anticipated; the failure of our customers to grow and expand as we anticipated; the effects of natural or other events beyond our control, including the effects political unrest, war or terrorist activities may have on us or the economy; the economic environment's effect on us or our customers; the growth of, acceptance of and the demand for our products and technologies in various markets and geographical regions, including cable, satellite, consumer electronics, retail, and digital media and interactive technology; our successful integration of the Ecolink and RCS assets and business lines; our inability to add profitable complementary products which are accepted by the marketplace; our inability to attract and retain a quality workforce at adequate levels in all regions of the world, and particularly Asia; our inability to continue to maintain our operating costs at acceptable levels through our cost containment efforts; an unfavorable ruling in any or all of the litigation matters to which we are party; our inability to continue selling our products or licensing our technologies at higher or profitable margins; our inability to obtain orders or maintain our order volume with new and existing customers; our inability to develop new and innovative technologies and products that are accepted by our customers; the sale of our Guangzhou facility not occurring as or within the time frame anticipated by management; our inability to successfully and profitably restructure our manufacturing facilities and activities; possible dilutive effect our stock incentive programs

may have on our earnings per share and stock price; the continued ability to identify and execute on opportunities that maximize stockholder value, including the effects repurchasing the company's shares have on the company's stock value; our inability to continue to obtain adequate quantities of component parts or secure adequate factory production capacity on a timely basis; and other factors listed from time to time in our press releases and filings with the Securities and Exchange Commission.

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ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are exposed to various market risks, including interest rate and foreign currency exchange rate fluctuations. We have established policies, procedures and internal processes governing our management of these risks and the use of financial instruments to mitigate our risk exposure.

Interest Rate Risk

We are exposed to interest rate risk related to our debt. From time to time we borrow amounts on our Credit Line for working capital and other liquidity needs. Under our Amended Credit Agreement, we may elect to pay interest on outstanding borrowings on our Credit Line based on LIBOR or a base rate (based on the prime rate of U.S. Bank) plus an applicable margin as defined in the Amended Credit Agreement. Accordingly, changes in interest rates would impact our results of operations in future periods. A 100 basis point increase in interest rates would have an approximately $0.6 million annual impact on net income based on our outstanding line of credit balance at June 30, 2017.

We cannot make any assurances that we will not need to borrow additional amounts in the future or that funds will be extended to us under comparable terms or at all. If funding is not available to us at a time when we need to borrow, we would have to use our cash reserves, including potentially repatriating cash from foreign jurisdictions, which may have a material adverse effect on our operating results, financial position and cash flows.

Foreign Currency Exchange Rate Risk

At June 30, 2017, we had wholly-owned subsidiaries in Argentina, Brazil, Cayman Islands, France, Germany, Hong Kong, India, Italy, Japan, Korea, Mexico, the Netherlands, the PRC, Singapore, Spain and the United Kingdom. We are exposed to foreign currency exchange rate risk inherent in our sales commitments, anticipated sales, anticipated purchases, operating expenses, assets and liabilities denominated in currencies other than the U.S. Dollar. The most significant foreign currencies to our operations are the Chinese Yuan Renminbi, Euro, British Pound, Argentinian Peso, Mexican Peso, Brazilian Real, Indian Rupee and Japanese Yen. Our most significant foreign currency exposure is to the Chinese Yuan Renminbi as this is the functional currency of our China-based factories where the majority of our products are manufactured. If the Chinese Yuan Renminbi were to strengthen against the U.S. Dollar, our manufacturing costs would increase. We are generally a net payor of the Euro, Mexican Peso, Indian Rupee and Japanese Yen and therefore benefit from a stronger U.S. Dollar and are adversely affected by a weaker U.S. Dollar relative to the foreign currency. For the British Pound, Argentinian Peso and Brazilian Real, we are generally a net receiver of the foreign currency and therefore benefit from a weaker U.S. Dollar and are adversely affected by a stronger U.S. Dollar relative to the foreign currency. Even where we are a net receiver, a weaker U.S. Dollar may adversely affect certain expense figures taken alone.

From time to time, we enter into foreign currency exchange agreements to manage the foreign currency exchange rate risks inherent in our forecasted income and cash flows denominated in foreign currencies. The terms of these foreign currency exchange agreements normally last less than nine months. We recognize the gains and losses on these foreign currency contracts in the same period as the remeasurement losses and gains of the related foreign currency-denominated exposures.

It is difficult to estimate the impact of fluctuations on reported income, as it depends on the opening and closing rates, the average net balance sheet positions held in a foreign currency and the amount of income generated in local currency. We routinely forecast what these balance sheet positions and income generated in local currency may be and we take steps to minimize exposure as we deem appropriate. Alternatively, we may choose not to hedge the foreign currency risk associated with our foreign currency exposures, primarily if such exposure acts as a natural foreign currency hedge for other offsetting amounts denominated in the same currency or the currency is difficult or too expensive to hedge. We do not enter into any derivative transactions for speculative purposes.

The sensitivity of earnings and cash flows to variability in exchange rates is assessed by applying an approximate range of potential rate fluctuations to our assets, obligations and projected results of operations denominated in foreign currency with all other variables held constant. The analysis includes all of our foreign currency contracts offset by the underlying exposures. Based on our overall foreign currency rate exposure at June 30, 2017, we believe that movements in foreign currency rates may have a material effect on our financial position and results of operations. We estimate that if the exchange rates for the Chinese Yuan Renminbi, Euro, British Pound, Argentinian Peso, Mexican

Peso, Brazilian Real, Indian Rupee and Japanese Yen relative to the U.S. Dollar fluctuate 10% from June 30, 2017, net income in the third quarter of 2017 would fluctuate by approximately $10.4 million.

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ITEM 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

Exchange Act Rule 13a-15(d) defines "disclosure controls and procedures" to mean controls and procedures of a company that are designed to ensure that information required to be disclosed by the company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Commission's rules and forms. The definition further states that disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that the information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the company's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

An evaluation was performed under the supervision and with the participation of our management, including our principal executive and principal financial officers, of the effectiveness of the design and operation of our disclosure controls and procedures as of the end of the period covered by this report. Based on that evaluation, our principal executive and principal financial officers have concluded that our disclosure controls and procedures were effective, as of the end of the period covered by this report, to provide reasonable assurance that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in Securities and Exchange Commission rules and forms and is accumulated and communicated to our management to allow timely decisions regarding required disclosures.

Changes in Internal Control Over Financial Reporting

There have been no changes in internal controls or in other factors that may significantly affect our internal controls during the fiscal quarter covered by this Quarterly Report on Form 10-Q.

PART II. OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

We are subject to lawsuits arising out of the conduct of our business. The discussion of our litigation matters contained in "Notes to Consolidated Financial Statements - Note 10" is incorporated herein by reference.

ITEM 1A. RISK FACTORS

The reader should carefully consider, in connection with the other information in this report, the factors discussed in "Part I, Item
1A: Risk Factors" of the Company's 2016 Annual Report on Form 10-K incorporated herein by reference. These factors may cause our actual results to differ materially from those stated in forward-looking statements contained in this document and elsewhere.

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

During the three months ended June 30, 2017, we repurchased 54,350 shares of our issued and outstanding common stock for $3.5 million. We make stock repurchases under ongoing and systematic programs approved by our Board of Directors to manage the dilution created by shares issued under our stock incentive plans or when we deem a repurchase is a good use of our cash and the price to be paid is at or below a threshold approved by our Board from time to time. On June 30, 2017, we had 148,853 shares available for repurchase on the open market under the Board's authorizations. On July 26, 2017, our Board increased these repurchase authorizations by 51,147 shares bringing the total authorizations as of the approval date to 200,000 shares. Shares may also be tendered by employees to satisfy tax withholding obligations in connection with the vesting of restricted stock.

The following table sets forth, for the three months ended June 30, 2017, our total stock repurchases, average price paid per share and the maximum number of shares that may yet be purchased on the open market under our plans or programs:

Period	Total Number of Shares Purchased (1)	Weighted Average Price Paid per Share (2)	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs (3)
April 1, 2017 - April 30, 2017	1,354	$ 67.89	—	200,000
May 1, 2017 - May 31, 2017	52,392	64.20	51,147	148,853
June 1, 2017 - June 30, 2017	604	67.11	—	148,853
Total	54,350	$ 64.33	51,147	148,853

(1) Of the repurchases in April, May and June, 1,354, 1,245 and 604 shares, respectively, represent common shares of the company that were owned and tendered by employees to satisfy tax withholding obligations in connection with the vesting of restricted shares.

(2) For shares tendered in connection with the vesting of restricted shares, the average price paid per share is an average calculated using the daily high and low of the Company's common stock at the time of vesting.

(3) The Company may purchase shares from time to time in open market purchases. The Company may make all or part of the purchases pursuant to accelerated share repurchases or Rule 10b5-1 plans.

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ITEM 6. EXHIBITS

10.1	Ninth Amendment to Amended and Restated Credit Agreement dated as of June 20, 2017 between Universal Electronics Inc. and U.S. Bank National Association (filed herewith)
31.1	Rule 13a-14(a) Certifications of Paul D. Arling, Chief Executive Officer (principal executive officer) of Universal Electronics Inc.
31.2	Rule 13a-14(a) Certifications of Bryan M. Hackworth, Chief Financial Officer (principal financial officer and principal accounting officer) of Universal Electronics Inc.
32	Section 1350 Certifications of Paul D. Arling, Chief Executive Officer (principal executive officer) of Universal Electronics Inc., and Bryan M. Hackworth, Chief Financial Officer (principal financial officer and principal accounting officer) of Universal Electronics Inc. pursuant to 18 U.S.C. Section 1350
101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

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SIGNATURES

Pursuant to the requirement of Section 13 or 15(d) 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.

Dated: August 8, 2017	UNIVERSAL ELECTRONICS INC.	
	By:	/s/ Bryan M. Hackworth
		Bryan M. Hackworth
		Chief Financial Officer (principal financial officer and principal accounting officer)

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EXHIBIT INDEX

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101.INS	XBRL Instance Document
101.SCH	XBRL Taxonomy Extension Schema Document
101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

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