Ultra Clean Holdings, Inc.
Form 10-Q
August 08, 2018

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 29, 2018

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to

Commission file number 000-50646

Ultra Clean Holdings, Inc.

(Exact name of registrant as specified in its charter)

Delaware	61-1430858
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
26462 Corporate Avenue, Hayward, California	94545
(Address of principal executive offices)	(Zip Code)

(510) 576-4400

Registrant's telephone number, including area code

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 the past 90 days. Yes No

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 for such shorter period that the registrant was required to submit and post such files). Yes No

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

Large accelerated filer	Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company)	Smaller reporting company
	Emerging growth company

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

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

Number of shares outstanding of the issuer's common stock as of July 27, 2018: 38,935,221

ULTRA CLEAN HOLDINGS, INC.

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PART I. FINANCIAL INFORMATION

ITEM 1. Financial Statements
ULTRA CLEAN HOLDINGS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited; in thousands, except share and per share amounts)

	June 29, 2018	December 29, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$ 141,146	$ 68,306
Accounts receivable, net of allowance of $67 and $69, respectively	98,608	90,213
Inventories	228,570	236,840
Prepaid expenses and other	15,115	12,089
Total current assets	483,439	407,448
Equipment and leasehold improvements, net	38,769	32,246
Goodwill	85,248	85,248
Purchased intangibles, net	29,392	31,587
Deferred tax assets, net	5,067	4,951
Other non-current assets	1,830	1,932
Total assets	$ 643,745	$ 563,412
LIABILITIES AND STOCKHOLDERS’ EQUITY		
Current liabilities:		
Bank borrowings	$ 54,826	$ 12,381
Accounts payable	113,803	173,521
Accrued compensation and related benefits	9,416	10,788
Deferred rent, current portion	680	670
Other current liabilities	10,143	9,987
Total current liabilities	188,868	207,347
Bank borrowings, net of current portion	—	39,893
Deferred tax liability	9,868	9,981
Deferred rent and other liabilities	5,682	5,886
Total liabilities	204,418	263,107
Commitments and contingencies (See Note 9)		
Stockholders’ equity:		
Preferred stock — $0.001 par value, 10,000,000 authorized; none outstanding	—	—
Common stock — $0.001 par value, 90,000,000 authorized; 38,926,652 and 33,664,940 shares issued and outstanding, in 2018 and 2017, respectively	39	34
Additional paid-in capital	285,390	188,639

Common shares held in treasury, at cost, 601,944 shares in 2018 and 2017	(3,337)	(3,337)
Retained earnings	156,823	113,122
Accumulated other comprehensive gain	412	1,847
Total stockholders' equity	439,327	300,305
Total liabilities and stockholders' equity	$643,745	$ 563,412

(See accompanying Notes to Condensed Consolidated Financial Statements)

ULTRA CLEAN HOLDINGS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited; in thousands, except per share data)

	Three Months Ended		Six Months Ended	
	June 29, 2018	June 30, 2017	June 29, 2018	June 30, 2017
Sales	$290,213	$228,261	$605,055	$432,855
Cost of goods sold	244,148	184,890	510,186	351,989
Gross profit	46,065	43,371	94,869	80,866
Operating expenses:				
Research and development	2,915	2,774	5,944	5,680
Sales and marketing	3,630	3,351	7,435	6,402
General and administrative	16,856	12,841	31,918	24,606
Total operating expenses	23,401	18,966	45,297	36,688
Income from operations	22,664	24,405	49,572	44,178
Interest and other income (expense), net	(809)	(1,120)	(483)	(2,058)
Income before provision for income taxes	21,855	23,285	49,089	42,120
Income tax provision	2,895	3,106	5,388	7,600
Net income	$18,960	$20,179	$43,701	$34,520
Net income per share:				
Basic	$0.49	$0.60	$1.16	$1.04
Diluted	$0.48	$0.59	$1.14	$1.01
Shares used in computing net income per share:				
Basic	38,802	33,433	37,763	33,247
Diluted	39,297	34,064	38,418	34,017

(See accompanying Notes to Condensed Consolidated Financial Statements)

ULTRA CLEAN HOLDINGS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited; in thousands)

	Three Months Ended		Six Months Ended	
	June 29, 2018	June 30, 2017	June 29, 2018	June 30, 2017
Net income	$18,960	$20,179	$43,701	$34,520
Other comprehensive income:				
Change in cumulative translation adjustment	(799)	591	(463)	689
Cash flow hedges:				
Change in fair value of derivatives	(71)	679	(62)	692
Adjustment for net gain (loss) realized and included in net income	(24)	—	(910)	7
Total change in unrealized gain (loss) on derivative instruments	(95)	679	(972)	699
Other comprehensive income (loss), net of tax	(894)	1,270	(1,435)	1,388
Comprehensive income	$18,066	$21,449	$42,266	$35,908

(See accompanying Notes to Condensed Consolidated Financial Statements)

ULTRA CLEAN HOLDINGS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited; in thousands)

	Six Months Ended	
	June 29, 2018	June 30, 2017
Cash flows from operating activities:		
Net income	$43,701	$34,520
Adjustments to reconcile net income to net cash provided by (used for) operating activities:		
Depreciation and amortization	2,917	2,586
Amortization of finite-lived intangibles	2,195	2,462
Amortization of debt issuance costs	76	76
Stock-based compensation	4,920	2,762
Change in the fair value of financial instruments	(228)	619
Loss on the disposal of fixed assets	201	—
Changes in assets and liabilities:		
Accounts receivable	(8,758)	(26,717)
Inventories	7,766	(35,174)
Prepaid expenses and other	(3,558)	13
Deferred income taxes	(113)	(40)
Other non-current assets	(313)	(337)
Accounts payable	(59,490)	31,350
Accrued compensation and related benefits	(1,332)	3,010
Income taxes payable	(3,933)	3,993
Other liabilities	3,903	1,058
Net cash provided by (used for) operating activities	(12,046)	20,181
Cash flows from investing activities:		
Purchases of equipment and leasehold improvements	(9,666)	(5,770)
Net cash used for investing activities	(9,666)	(5,770)
Cash flows from financing activities:		
Proceeds from bank borrowings	21,886	5,205
Proceeds from issuance of common stock	94,454	1,677
Principal payments on bank borrowings	(19,148)	(12,607)
Employees' taxes paid upon vesting of restricted stock units	(2,618)	(1,810)
Net cash provided by (used for) financing activities	94,574	(7,535)
Effect of exchange rate changes on cash and cash equivalents	(22)	141
Net increase in cash and cash equivalents	$72,840	$7,017
Cash and cash equivalents at beginning of period	68,306	52,465
Cash and cash equivalents at end of period	$141,146	$59,482
Supplemental cash flow information:		
Income taxes paid	$9,200	$3,797
Income tax refunds	$43	$25

Interest paid	$942	$2,259
Non-cash investing and financing activities:		
Equipment and leasehold improvements purchased included in accounts payable	$2,575	$1,475

(See accompanying Notes to Condensed Consolidated Financial Statements)

ULTRA CLEAN HOLDINGS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Organization and Significant Accounting Policies

Organization — Ultra Clean Holdings, Inc. (the "Company" or "UCT") was founded in November 2002 for the purpose of acquiring Ultra Clean Technology Systems and Service, Inc. Ultra Clean Technology Systems and Service, Inc. was founded in 1991 by Mitsubishi Corporation and was operated as a subsidiary of Mitsubishi until November 2002, when it was acquired by UCT. UCT became a publicly traded company in March 2004. Ultra Clean Technology (Shanghai) Co., Ltd ("UCTS") and Ultra Clean Micro-Electronics Equipment (Shanghai) Co., Ltd. ("UCME") were established in 2005 and 2007, respectively, to facilitate the Company's operations in China. In December 2015, UCTS merged into UCME. Ultra Clean Asia Pacific, Pte, Ltd. (Singapore) was established in fiscal year 2008 to facilitate the Company's operations in Singapore. In July 2012, UCT acquired American Integration Technologies LLC ("AIT") to add to the Company's existing customer base in the semiconductor and medical spaces and to provide additional manufacturing capabilities. In February 2015, UCT acquired Marchi Thermal Systems, Inc. ("Marchi"), a designer and manufacturer of specialty heaters, thermocouples and temperature controllers. Marchi delivers flexible heating elements and thermal solutions to our customers. The Company believes heaters are increasingly critical in equipment design for the most advanced semiconductor nodes. In July 2015, UCT acquired MICONEX s.r.o. ("Miconex"), a privately-held provider of advanced precision fabrication of plastics, to expand the Company's capabilities with existing customers. In May 2018, Marchi and Miconex changed their names to UCT Thermal Solutions, Inc. ("Thermal") and to UCT Fluid Delivery Solutions s.r.o ("FDS"), respectively.

Basis of Presentation — The unaudited condensed consolidated financial statements included in this quarterly report on Form 10-Q include the accounts of the Company and its wholly-owned subsidiaries and have been prepared in accordance with U.S. generally accepted accounting principles ("GAAP"). This financial information reflects all adjustments which are, in the opinion of the Company, normal, recurring and necessary for the fair financial statement presentation for the dates and periods presented. Certain information and footnote disclosures normally included in our annual financial statements, prepared in accordance with GAAP, have been condensed or omitted. The Company's December 29, 2017 balance sheet data were derived from its audited financial statements as of that date.

Principles of Consolidation — The Company's condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries and all intercompany accounts and transactions have been eliminated in consolidation. The Company uses a 52-53 week fiscal year ending on the Friday nearest December 31. All references to quarters refer to fiscal quarters and all references to years refer to fiscal years.

Foreign Currency Translation and Remeasurement — The Company has one foreign subsidiary whose functional currency is not its local currency or the U.S. dollar. The Company remeasures the monetary assets and liabilities of this subsidiary into its functional currency. Gains and losses from these remeasurements are recorded in interest and other income (expense), net. The Company then translates the assets and liabilities of this subsidiary into the U.S. dollar. Gains and losses from these translations are recognized in foreign currency translation included in accumulated other comprehensive income (AOCI) within stockholders' equity. For the Company's foreign subsidiaries where the U.S. dollar is the functional currency, any gains and losses resulting from the translation of the assets and liabilities of these subsidiaries are recorded in interest and other income (expense), net.

Use of Accounting Estimates — The presentation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and disclosures of contingent liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Such estimates and assumptions include reserves on inventory, valuation of deferred tax assets and impairment of goodwill and other long-lived assets. The Company bases its estimates and judgments on historical experience and on various other assumptions that it believes are reasonable under the circumstances. However, future events are subject to change and the best estimates and judgments routinely require adjustment. Actual amounts may differ from those estimates.

Concentration of Credit Risk — Financial instruments which subject the Company to concentrations of credit risk consist principally of cash and cash equivalents and accounts receivable. The Company sells its products primarily to semiconductor capital equipment manufacturers in the United States. The Company performs credit evaluations of its customers' financial condition and generally requires no collateral.

Fair Value of Measurements — The Company measures its cash equivalents, interest rate swap contract and forward contracts at fair value on a recurring basis. Fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. As such, fair value is a market-based measurement that is determined based on assumptions that market participants would use in pricing an asset or a liability. Assets and liabilities recorded at fair value are measured and classified in accordance with a three-tier fair value hierarchy based on the observability of the inputs available in the market used to measure fair value:

Level 1 — Observable inputs that reflect quoted prices (unadjusted) for identical assets or liabilities in active markets.

Level 2 — Inputs that are based upon quoted prices for similar instruments in active markets, quoted prices for identical or similar instruments in markets that are not active, and model-based valuation techniques for which all significant inputs are observable in the market or can be derived from observable market data. Where applicable, these models project future cash flows and discount the future amounts to a present value using market-based observable inputs including interest rate curves, foreign exchange rates, and credit ratings.

Level 3 — Unobservable inputs that are supported by little or no market activities.

The fair value hierarchy requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. The following table summarizes, for assets or liabilities measured at fair value, the respective fair value and the classification by level of input within the fair value hierarchy (in thousands):

		Fair Value Measurement at Reporting Date Using		
Description	June 29, 2018	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
Other assets:				
Interest rate swap	$ 14	$ —	$ 14	$ —
Forward contracts	$ 457	$ —	$ 457	$ —

		Fair Value Measurement at Reporting Date Using		
Description	December 29, 2017	Quoted Prices in Active Markets for Identical Assets	Significant Other Observable	Significant Unobservable Inputs

		(Level 1)	Inputs (Level 2)	(Level 3)
Other assets:				
Interest rate swap	$ 30	$ —	$ 30	$ —
Forward contracts	$ 1,302	$ —	$ 1,302	$ —

Derivative Financial Instruments — The Company recognizes derivative instruments as either assets or liabilities in the accompanying Condensed Consolidated Balance Sheets at fair value. The Company records changes in the fair value of the derivatives in the accompanying Condensed Consolidated Statements of Operations as interest and other income (expense), net, or as a component of AOCI in the accompanying Condensed Consolidated Balance Sheets.

Inventories — Inventories are stated at the lower of standard cost (which approximates actual cost on a first-in, first-out basis) or net realizable value. The Company evaluates the valuation of all inventories, including raw materials, work-in-process, finished goods and spare parts on a periodic basis. Obsolete inventory or inventory in excess of management's estimated usage is written-down to its estimated market value less costs to sell, if less than its cost. Inherent in the estimates of market value are management's estimates related to economic trends, future demand for products, and technological obsolescence of the Company's products.

Inventory write downs inherently involve judgments as to assumptions about expected future demand and the impact of market conditions on those assumptions. Although the Company believes that the assumptions it used in estimating inventory write downs are reasonable, significant changes in any one of the assumptions in the future could produce a significantly different result. There can be no assurances that future events and changing market conditions will not result in significant increases in inventory write downs.

Equipment and Leasehold Improvements, net — Equipment and leasehold improvements are stated at cost, or, in the case of equipment under capital leases, the present value of future minimum lease payments at inception of the related lease. Depreciation and amortization are computed using the straight-line method over the lesser of the estimated useful lives of the assets or the terms of the leases. Useful lives range from three to fifteen years.

Internal use software — Direct costs incurred to develop software for internal use are capitalized and amortized over an estimated useful life of three to five years. Costs related to the design or maintenance of internal use software are expensed as incurred. Capitalized internal use software is included in computer equipment and software.

Construction in progress — Construction in progress is related to the construction or development of property and equipment that has not yet been placed in service for their intended use and is, therefore, not depreciated. Construction in progress currently includes capitalized costs related to the Company's Enterprise Resource Planning ("ERP") implementation project.

Income Taxes — The Company utilizes the asset and liability method of accounting for income taxes, under which deferred taxes are determined based on the temporary differences between the financial statement and tax basis of assets and liabilities using tax rates expected to be in effect during the years in which the basis differences reverse. Deferred income taxes arise from temporary differences between the tax basis of assets and liabilities and their reported amounts in the financial statements, which will result in taxable or deductible amounts in the future. In evaluating our ability to realize our deferred tax assets within the jurisdiction from which they arise, we consider all available positive and negative evidence, including scheduled reversals of deferred tax liabilities, projected future taxable income, tax-planning strategies, and results of recent operations. In projecting future taxable income, we begin with historical results and incorporate assumptions about the amount of future state, federal, and foreign pretax operating income adjusted for items that do not have tax consequences. The assumptions about future taxable income require significant judgment and are consistent with the plans and estimates we are using to manage the underlying businesses. In evaluating the objective evidence that historical results provide, we consider recent cumulative income (loss). A valuation allowance is recorded when it is more likely than not that some of the deferred tax assets will not be realized.

The Company continued to maintain a full valuation allowance on its federal, state, and one of its Singapore subsidiary's deferred tax amounts as of June 29, 2018. Income tax positions must meet a more likely than not recognition threshold to be recognized. Income tax positions that previously failed to meet the more likely than not threshold are recognized in the first subsequent financial reporting period in which that threshold is met. Previously recognized tax positions that no longer meet the more likely than not threshold are derecognized in the first subsequent financial reporting period in which that threshold is no longer met. The Company recognizes potential accrued interest and penalties related to unrecognized tax benefits within the Condensed Consolidated Statements of Operations as income tax expense. The calculation of tax liabilities involves significant judgment in estimating the impact of uncertainties in the application of complex tax laws. Resolution of these uncertainties in a manner inconsistent with the Company's expectations could have a material impact on its results of operations and financial position. Management believes that it has adequately provided for any adjustments that may result from these examinations; however, the outcome of tax audits cannot be predicted with certainty.

The determination of the Company's tax provision is subject to judgments and estimates.

Revenue Recognition — See Note 3 to the Company's Condensed Consolidated Financial Statements.

Research and Development Costs — Research and development costs are expensed as incurred.

Net Income per Share — Basic net income per share is computed by dividing net income by the weighted average number of shares outstanding for the period. Diluted net income per share is calculated by dividing net income by the weighted average number of common shares outstanding and common equivalent shares from dilutive stock options and restricted stock using the treasury stock method, except when such shares are anti-dilutive. See Note 8 to the Company's Condensed Consolidated Financial Statements.

Segments — The Financial Accounting Standards Board's (FASB) guidance regarding disclosure about segments in an enterprise and related information establishes standards for the reporting by public business enterprises of information about reportable segments, products and services, geographic areas, and major customers. The method for determining what information to report is based on the manner in which management organizes the reportable segments within the Company for making operational decisions and assessments of financial performance. The Company's chief operating decision-maker is considered to be the Chief Executive Officer. The Company operates in one operating segment, and therefore, has one reportable segment.

Business Combinations — The Company recognizes assets acquired (including goodwill and identifiable intangible assets) and liabilities assumed at fair value on the acquisition date. Subsequent changes to the fair value of such assets acquired and liabilities assumed are recognized in earnings, after the expiration of the measurement period, a period not to exceed 12 months from the acquisition date. Acquisition-related expenses and acquisition-related restructuring costs are recognized in earnings in the period in which they are incurred.

Stock-Based Compensation Expense

The Company maintains stock-based compensation plans which allow for the issuance of equity-based awards to executives, directors and certain employees. These equity-based awards include stock options, restricted stock awards (“RSAs”) and restricted stock units (“RSUs”) which can be either time-based or performance-based. The Company has not granted stock options to its employees since fiscal year 2010. The Company also maintains an employee stock purchase plan that provides for the issuance of shares to all eligible employees of the Company at a discounted price.

Stock-based compensation expense includes compensation costs related to estimated fair values of stock options and awards granted. The estimated fair value of the Company’s equity-based awards, net of expected forfeitures, is amortized on a straight-line basis over the awards’ vesting period, typically three years for RSUs and one year for RSAs, and is adjusted for subsequent changes in estimated forfeitures related to all equity-based awards and performance as it relates to performance-based RSUs. The Company applies the fair value recognition provisions based on the FASB’s guidance regarding stock-based compensation.

Employee Stock Purchase Plan

The Company also maintains an employee stock purchase plan (“ESPP”) that provides for the issuance of shares to all eligible employees of the Company at a discounted price. Under the ESPP, substantially all employees may purchase the Company’s common stock through payroll deductions at a price equal to 95 percent of the fair market value of the Company’s stock at the end of each applicable purchase period.

Restricted Stock Units and Restricted Stock Awards

The Company grants RSUs to employees and RSAs to non-employee directors as part of the Company’s long term equity compensation plan.

Restricted Stock Units — RSUs are granted to employees with a per share or unit purchase price of zero dollars and either have time based or performance based vesting. RSUs typically vest over three years, subject to the employee’s continued service with the Company. For purposes of determining compensation expense related to these RSUs, the fair value is determined based on the closing market price of the Company’s common stock on the date of award. The expected cost of the grant is reflected over the service period, and is reduced for estimated forfeitures.

There were no RSUs and performance stock units (“PSUs”) granted during the quarter ended June 29, 2018. During the quarter ended March 30, 2018, the Company granted 174,900 RSUs, with a weighted average fair value of $19.57 per share, and granted 87,050 performance stock units with a weighted average fair value of $19.25 per share.

During the six months ended June 29, 2018, 135,753 vested shares were withheld to satisfy withholding tax obligations, resulting in the net issuance of 448,439 shares. As of June 29, 2018, approximately $11.5 million of stock-based compensation cost, net of estimated forfeitures, related to RSUs and PSUs remains to be amortized over a weighted average period of 1.5 years. As of June 29, 2018, a total of 1,249,702 RSUs and PSUs remain outstanding with an aggregate intrinsic value of $20.7 million and a weighted average remaining contractual term of 1.1 years.

Restricted Stock Awards — As of June 29, 2018, a total of 38,010 RSAs were outstanding. The total unamortized expense of the Company’s unvested restricted stock awards as of June 29, 2018 was $0.5 million.

The following table summarizes the Company’s RSU, PSU and RSA activity for the six months ended June 29, 2018:

	Shares	Aggregate Fair Value (in thousands)
Unvested restricted stock units and restricted stock awards at December 29, 2017	1,676,312	$ 38,706
Granted	299,960	
Vested	(629,192)	
Forfeited	(97,378)	
Unvested restricted stock units and restricted stock awards at June 29, 2018	1,249,702	$ 20,745
Vested and expected to vest restricted stock units and restricted stock awards at June 29, 2018	1,069,087	$ 17,747

The following table shows the Company’s stock-based compensation expense included in the Condensed Consolidated Statements of Operations (in thousands):

	Three Months Ended		Six Months Ended	
	June 29, 2018	June 30, 2017	June 29, 2018	June 30, 2017
Cost of sales (1)	$ 517	$ 258	$ 1,023	$ 601
Research and development	10	47	71	100
Sales and marketing	193	97	396	221
General and administrative	1,636	978	3,430	1,840
	2,356	1,380	4,920	2,762
Income tax benefit	(312)	(184)	(540)	(498)
Stock-based compensation expense, net of tax	$ 2,044	$ 1,196	$ 4,380	$ 2,264

(1) Stock-based compensation expense capitalized in inventory for the three and six months ended June 29, 2018 and June 30, 2017 was not significant.

Recently Adopted Accounting Pronouncements

Effective December 30, 2017, the Company adopted FASB Accounting Standards Codification (ASC) 606, Revenue from Contracts with Customers (Topic 606) using the modified retrospective approach, which requires the recognition

of the cumulative effect of initially applying the standard (if any) as an adjustment to the opening retained earnings of the fiscal year beginning December 30, 2017. The adoption of Topic 606 did not result in the recognition of a cumulative adjustment to the opening retained earnings under the modified retrospective approach, nor did it have a material effect on the Company's financial position or results of operations. The adoption of Topic 606 did, however, result in the addition of required disclosures within the notes to financial statements. This new standard replaced the previous revenue recognition guidance under U.S. GAAP. See Note 3, Revenue Recognition in Notes to Condensed Consolidated Financial Statements.

Our implementation team consisted of senior leadership from finance, legal, sales and operations with periodic progress reporting to management and to the audit committee of our board of directors. Implementation consisted of a review of the Company's significant contracts and an evaluation of our systems and control environment to support additional disclosures under the new standard, as well as updates to our policies and procedures.

During our assessment, we considered whether the adoption would require a transition from point-in-time revenue recognition to an over-time approach for products produced by us without an alternative use, which would result in acceleration of revenue. We concluded based on enforceable rights or prevailing terms and conditions included in the agreements with our customers, an enforceable right of payment that includes a reasonable profit throughout the duration of the contract does not exist. Therefore, we will remain at a point-in-time approach and record revenue at the point control transfers to our customers.

Beginning fiscal 2018, the Company adopted ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments, which clarifies classification of seven different cash receipts and payments on statement of cash flows and on how the predominance principle should be applied. The adoption of this guidance did not have an impact on the Company's consolidated financial statements.

Beginning fiscal 2018, the Company adopted ASU 2017-01, Business Combinations (Topic 805): Clarifying the Definition of a Business, which clarifies the definition of a business to assist entities with evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The impact of the adoption on the Company's financial position and results of operations will be dependent upon future acquisitions or disposals, if any.

Beginning fiscal 2018, the Company adopted ASU No. 2017-09, Stock Compensation: Scope of Modification Accounting, which clarifies when changes to the terms or conditions of a share-based payment award must be accounted for as a modification. The new guidance requires the application of modification accounting if the value, vesting conditions or classification of the award changes. The impact of the adoption of this guidance will depend on whether the Company makes any future modifications of share-based payment awards.

Recent Accounting Pronouncements Not Yet Adopted

In February 2016, the FASB issued Accounting Standards Update (ASU) No. 2016-02, Leases (Topic 842). Topic 842 supersedes the lease recognition requirements in ASC Topic 840, Leases. The guidance specifies that an entity who is a lessee under lease agreements should recognize lease assets and lease liabilities for those leases classified as operating leases under previous FASB guidance. The guidance is effective beginning in the first quarter of 2019. Early adoption is permitted. In transition, lessees and lessors are required to recognize and measure leases at the beginning of the earliest period presented using a modified retrospective approach. The Company is evaluating the impact of adopting this guidance on the Company's consolidated financial statements. The Company currently expects that its operating lease commitments will be subject to the new standard and recognized as right-of-use asset and operating lease liability upon adoption of this standard, which will increase the total assets and total liabilities that it reports relative to such amounts prior to adoption.

In January 2017, the FASB issued Accounting Standards Update No. 2017-04, Intangibles-Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment, which requires companies to perform goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. The amendment will be effective for the Company beginning in its first quarter of fiscal year 2020. The amendment is required to be adopted prospectively. Early adoption is permitted. The Company is evaluating the impact of adopting this amendment to its consolidated financial statements.

In August 2017, the FASB issued ASU 2017-12, Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities, which improves the financial reporting of hedging relationships to better portray the economic results of an entity's risk management activities in its financial statements and simplifies the application of hedge accounting. This standard will be effective for the Company beginning in its first quarter of fiscal year 2019

with early adoption permitted. The Company is evaluating the impact of adopting this amendment to its consolidated financial statements and related disclosures.

2. Financial Instruments

Derivative Financial Instruments

The Company utilizes foreign currency forward contracts with a local financial institution in the Czech Republic to reduce the risk that its cash flows and earnings of its FDS subsidiary will be adversely affected by foreign currency exchange rate fluctuations and uses certain interest rate derivative contracts to hedge interest rate exposures on existing floating rate debt. The Company classifies its foreign currency forward contracts and interest rate derivative contracts primarily within Level 2 of the fair-value hierarchy discussed in Note 1 of the Company's Consolidated Financial Statements as the valuation inputs are based on quoted prices and market observable data of similar instruments. The Company does not use derivatives for speculative or trading purposes.

Cash Flow Hedges

In September 2015, the Company entered into an interest rate swap with East West Bank and City National Bank with a notional amount of $20.0 million pursuant to which the Company pays the counterparty a fixed rate of 0.99% and receives interest at a variable rate equal to the London Interbank Offered Rate (LIBOR) rate the Company is required to pay under its term loan, or 1.98%, as of June 29, 2018. This interest rate swap effectively locks in a fixed interest rate of 2.99% on $4.7 million of the $7.4 million term loan as of June 29, 2018, with a decreasing notional amount based on prorated quarterly principal payments over the remaining period of

the term loan. Gains or losses on the effective portion of a cash flow hedge are reflected as a component of AOCI and subsequently recorded to interest and other income (expense) when the hedged transactions are realized. If the hedged transactions become probable of not occurring, the corresponding amounts in AOCI would be immediately reclassified to interest and other income (expense), net. As of June 29, 2018, the effective portion of the Company's cash flow hedge before tax effect was less than $0.1 million, of which less than $0.1 million is expected to be reclassified from AOCI into earnings within the next 12 months.

Non-Designated Derivatives

A portion of FDS's forward contracts with a total notional amount of $4.7 million is not designated as a hedging instrument. The Company recognizes gains and losses on these contracts, as well any related costs, in interest and other income (expense), net.

The Company records all derivatives in the Condensed Consolidated Balance Sheets at fair value. The Company's accounting treatment for these derivative instruments is based on its hedge designation. The following tables show the Company's derivative instruments at gross fair value (in thousands) as of June 29, 2018 and December 29, 2017.

		June 29, 2018		
	Balance Sheet Location	Fair Value of Derivatives Designated as Hedge Instruments	Fair Value of Derivatives Not Designated as Hedge Instruments	Total Fair Value
Derivative assets and liabilities:				
Level 2:				
Interest rate swap	Prepaid expenses and other	$ 14	$ —	$ 14
Forward contracts	Prepaid expenses and other	$ 61	$ 223	$ 284
Forward contracts	Other non-current assets	$ 21	$ 152	$ 173

		December 29, 2017		
	Balance Sheet Location	Fair Value of Derivatives Designated as Hedge Instruments	Fair Value of Derivatives Not Designated as Hedge Instruments	Total Fair Value
Derivative assets and liabilities:				
Level 2:				
Interest rate swap	Prepaid expenses and other	$ 30	$ —	$ 30
Forward contracts	Prepaid expenses and other	$ 714	$ —	$ 714
Forward contracts	Other non-current assets	$ 588	$ —	$ 588

The effect of derivative instruments in cash flow hedging relationships on income and other comprehensive income (OCI) is summarized below (in thousands):

	Gains (Losses) Recognized in OCI on Derivatives Before Tax Effect (Effective Portion)			
	Three Months Ended		Six Months Ended	
	June 29, 2018	June 30, 2017	June 29, 2018	June 30, 2017
Derivatives in Cash Flow Hedging Relationship				
Interest rate swap	$ (21)	$ (2)	$ (36)	$ 11
Forward contracts	$ (82)	$ 841	$ (71)	$ 841

	Gains Reclassified from AOCI into Income (Effective Portion)				
		Three Months Ended		Six Months Ended	
	Income Statement Location	June 29, 2018	June 30, 2017	June 29, 2018	June 30, 2017
Derivatives in Cash Flow Hedging Relationship					
Interest rate swap	Interest and other income (expense), net	$11	$ —	$20	$ 7
Forward contracts	Cost of goods sold	$(35)	$ —	$(930)	$ —

There were no gains (losses) recognized in income on derivatives that are excluded from the effectiveness testing and ineffective portion of the cash flow hedge for the three and six months ended June 29, 2018 and June 30, 2017.

The effect of derivative instruments not designated as hedging instruments on income for the three and six months ended June 29, 2018 was $(0.6) million and none for the three and six months ended June 30, 2017.

3. Revenue Recognition

On December 30, 2017, the Company adopted Topic 606 using the modified retrospective method to value those contracts which were not completed as of December 30, 2017. The adoption of Topic 606 did not have a material effect on the Company's financial position or results of operations.

Revenue is recognized when control of the promised goods or services is transferred to the Company's customers, in an amount that reflects the consideration the Company expects to be entitled to in exchange for those goods or services. The Company assesses collectability based on the credit worthiness of the customer and past transaction history. The Company performs on-going credit evaluations of customers and generally does not require collateral from customers.

The Company operates in one operating and reportable segment as the nature of the Company's products and production processes, as well as type of customers and distribution methods, is consistent among all of the Company's products. The Company sells its products primarily to customers in the semiconductor capital equipment industry. The Company's revenues are highly concentrated, and we are therefore highly dependent upon a small number of customers. Typical payment terms with our customers range from thirty to sixty days.

The Company's most significant customers (having accounted for 10% or more of sales) and their related sales as a percentage of total sales were as follows:

	Three Months Ended		Six Months Ended	
	June 29, 2018	June 30, 2017	June 29, 2018	June 30, 2017
Lam Research Corporation	61.9 %	57.1 %	64.2 %	57.9 %
Applied Materials, Inc.	21.6	25.7	21.5	26.3
Total	83.5 %	82.8 %	85.7 %	84.2 %

Two customers' accounts receivable balances, Lam Research Corporation and Applied Materials, Inc., were individually greater than 10% of accounts receivable as of June 29, 2018 and as of December 29, 2017, and in the aggregate represented approximately 70.6% and 75.8% of accounts receivable, respectively.

The Company provides warranty on its products for a period of up to two years and provides for warranty costs at the time of sale based on historical activity. Determination of the warranty reserve requires the Company to make estimates of product return rates and expected costs to repair or replace the products under warranty. If actual return rates and/or repair and replacement costs differ significantly from these estimates, adjustments to recognize additional cost of sales may be required in future periods. The warranty reserve is included in other current liabilities on the

Condensed Consolidated Balance Sheets and are not considered significant.

The Company's products are manufactured at our facilities in the U.S.A., China, Singapore and the Czech Republic. See Note 10 for geographical revenue details. Sales to customers are initiated through a purchase order and are governed by our standard terms and conditions, written agreements, or both. Revenue is recognized when performance obligations under the terms of an agreement with a customer are satisfied; generally, this occurs with the transfer of control of our products. Transfer of control occurs at a specific point-in-time. Based on the enforceable rights included in our agreements or prevailing terms and conditions, products produced by the Company without an alternative use are not protected by an enforceable right of payment that includes a reasonable profit throughout the duration of the agreement. Sales with terms f.o.b. shipping point are recognized at the time of shipment. For sales transactions with terms f.o.b. destination, revenue is recorded when the product is delivered to the customer's site. Consignment sales are recognized in revenue at the earlier of the period that the goods are consumed or after a period of time subsequent to receipt by the customer as specified by terms of the agreement, provided control of the promised goods or services has transferred.

Revenue is measured as the amount of consideration we expect to receive in exchange for transferring goods or providing services. Sales, value-add, and other taxes we collect concurrent with revenue-producing activities are excluded from revenue. Certain of our customers may receive cash-based incentives, such as rebates or credits, which are accounted for as variable consideration. We estimate these amounts based on the expected amount to be provided to customers and reduce revenues recognized. As of June 29, 2018, an accrual for unpaid customer rebates of $0.7 million is included in accrued expenses on the Company's Condensed Consolidated Balance Sheet. The adoption of Topic 606 did not have a significant impact on our estimates for variable consideration.

4. Balance Sheet Information

Inventories consisted of the following (in thousands):

	June 29, 2018	December 29, 2017
Raw materials	$177,432	$ 183,457
Work in process	37,581	43,826
Finished goods	13,557	9,557
Total	$228,570	$ 236,840

Equipment and leasehold improvements, net, consisted of the following (in thousands):

	June 29, 2018	December 29, 2017
Computer equipment and software	$11,853	$ 11,672
Furniture and fixtures	3,355	3,318
Machinery and equipment	20,459	19,781
Leasehold improvements	24,006	22,839
Accumulated depreciation	(40,994)	(38,879)
	18,679	18,731
Construction in progress	20,090	13,515
Total	$38,769	$ 32,246

5. Goodwill and Purchased Intangible Assets

The Company's methodology for allocating the purchase price relating to purchase acquisitions is determined through established and generally accepted valuation techniques. Goodwill is measured as the excess of the cost of the acquisition over the sum of the amounts assigned to tangible and identifiable intangible assets acquired less liabilities

assumed. Goodwill and purchased intangible assets with indefinite useful lives are not amortized, but are reviewed for impairment at least annually and whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. The Company regularly monitors current business conditions and other factors including, but not limited to, adverse industry or economic trends and lower projections of profitability that may impact future operating results.

To test goodwill for impairment, the Company first performs a qualitative assessment to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying value. If it is concluded that this is the case, the Company then performs the two-step goodwill impairment test. Otherwise, the two-step goodwill impairment test is not required. Under the two-step goodwill impairment test, the Company would in the first step compare the estimated fair value of each reporting unit to its carrying value. The Company determines the fair value of each of its reporting units based on a weighting of income and market approaches. If the carrying value of a reporting unit exceeds its fair value, the Company would then perform the second step of the impairment test in order to determine the implied fair value of the reporting unit’s goodwill. If the Company determines that the carrying value of a reporting unit’s goodwill exceeds its implied fair value, the Company would record an impairment charge equal to the difference.

The evaluation of goodwill and intangible assets for impairment requires the exercise of significant judgment. In the event of future changes in business conditions, the Company will be required to reassess and update its forecasts and estimates used in future impairment analyses. If the results of these future analyses are lower than current estimates, a material impairment charge may result at that time. Details of goodwill and other intangible assets were as follows (in thousands):

	June 29, 2018			December 29, 2017		
	Goodwill	Intangible Assets	Total	Goodwill	Intangible Assets	Total
Carrying amount	$85,248	$ 29,392	$114,640	$85,248	$ 31,587	$116,835

Purchased Intangible Assets

Intangible assets are generally recorded in connection with a business acquisition. The Company evaluates the useful lives of its intangible assets each reporting period to determine whether events and circumstances require revising the remaining period of amortization. In addition, the Company reviews indefinite lived intangible assets for impairment when events or changes in circumstances indicate their carrying value may not be recoverable and tests definite lives intangible assets at least annually for impairment. Management considers such indicators as significant differences in product demand from the estimates, changes in the competitive and economic environment, technological advances, and changes in cost structure. Details of purchased intangible assets were as follows (in thousands):

	As of June 29, 2018			As of December 29, 2017			
	Gross Carrying Amount	Accumulated Amortization	Carrying Value	Gross Carrying Amount	Accumulated Amortization	Carrying Value	Useful Life
AIT							
Customer relationships	$19,000	$ (18,307)	$693	$19,000	$ (17,998)	$1,002	7
Tradename	1,900	(1,900)	—	1,900	(1,900)	—	6
Intellectual property/know-how	1,600	(1,371)	229	1,600	(1,257)	343	7
Thermal							
Customer relationships	9,900	(3,383)	6,517	9,900	(2,887)	7,013	10
Tradename	1,170	(1,170)	—	1,170	(1,170)	—	6
Intellectual property/know-how	12,300	(4,712)	7,588	12,300	(4,023)	8,277	8-12
FDS							
Customer relationships	8,800	(3,422)	5,378	8,800	(2,835)	5,965	7.5
UCT							
Tradename	8,987	—	8,987	8,987	—	8,987	*
Total	$63,657	$ (34,265)	$29,392	$63,657	$ (32,070)	$31,587	

* The Company concluded that the UCT tradename intangible asset life is indefinite and is therefore not amortized but is reviewed for impairment at least annually and whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable.

The Company amortizes its intellectual property/know-how and customer relationships intangible assets for Thermal and FDS on a straight-line basis with an estimated economic life of the assets ranging from 7 to 12 years. Amortization expense was approximately $1.2 million for the three months ended June 29, 2018 and June 30, 2017. Amortization expense is charged to general and administrative expense. As of June 29, 2018, future estimated amortization expense is expected to be as follows (in thousands):

	Amortization Expense
2018 (remaining in year)	$ 2,196
2019	4,040
2020	3,543
2021	3,543
2022	3,543
Thereafter	3,540
Total	$ 20,405

6. Borrowing Arrangements

The Company has credit facilities in the U.S. and Czech Republic that expire on February 2, 2019 and March 31, 2020, respectively. The Company and certain of its subsidiaries have agreed to secure all of their obligations under a credit agreement (the "Credit Agreement") by granting a first priority lien in substantially all of their respective personal property assets (subject to certain exceptions and limitations).

As of June 29, 2018, the interest rates on the outstanding Term Loan and Revolving Credit facility were 3.98% (2.0% fixed and 1.98% variable based on LIBOR) and 4.25% fixed, respectively. In order to manage interest rate risk on the variable component of the Term Loan the Company entered into an interest rate swap with the Lenders in September 2015 with a total notional amount of $20.0 million pursuant to which the Company pays the counterparty a fixed rate of 0.99% and receives interest at a variable rate equal to the LIBOR rate the Company is required to pay under its Term Loan, or 1.98%, as of June 29, 2018. This interest rate swap effectively locked in a fixed interest rate of 2.99% on $4.7 million of the $7.4 million term loan balance outstanding as of June 29, 2018, with a decreasing notional amount based on principal payments over the remaining period of the term loan.

The Credit Agreement requires the Company to maintain certain financial covenants including a consolidated fixed charge coverage ratio (as defined in the Credit Agreement) of at least 1.25 to 1.00 starting with the end of the first quarter of fiscal 2015 and a consolidated leverage ratio (as defined in the Credit Agreement) no greater than 3.5 to 1.00 starting with the end of the first quarter of fiscal 2015. The Credit Agreement also includes other customary affirmative and negative covenants. In December 2015, the Credit Agreement was amended to add a covenant requiring the Company to maintain a minimum cash balance of $35.0 million at the end of each quarter. The Company was in compliance with all covenants for the quarter ended June 29, 2018.

The fair value of the Company's long term debt was based on Level 2 inputs, and fair value was determined using quoted prices for similar liabilities in inactive markets. The fair value of the Company's outstanding borrowings under the Company's revolving credit facility was based on Level 2 inputs, and fair value was determined using inputs other than quoted prices that are observable, specifically, discounted cash flows of expected payments at current borrowing rates. The Company's carrying value approximates fair value for the Company's long term debt and revolving credit facility.

As of June 29, 2018, the Company had outstanding amounts under the Term Loan and Revolving Credit Facility of $7.4 million and $39.9 million, respectively, which are gross of unamortized debt issuance costs of $0.1 million, for a total debt balance with this credit facility of $47.2 million.

As of June 29, 2018, FDS had outstanding amount under a revolving credit facility of 6.5 million euros (approximately $7.6 million) with an interest rate of 1.3% plus a variable rate based on the Euro Interbank Offered Rate.

As of June 29, 2018, the Company's total bank debt was $54.9 million. As of June 29, 2018, the Company had $0.1 million and 1.8 million euros (approximately $2.0 million) available to borrow on our revolving credit facilities in the U.S. and Czech Republic, respectively.

7. Income Tax

On December 22, 2017, the U.S. government enacted the Tax Cuts and Jobs Act of 2017 (TCJA). The TCJA significantly revised the future ongoing U.S. corporate income tax by, among other things, lowering U.S. corporate

income tax rates from 35% to 21% and implementing a territorial tax system. Other provisions included an immediate deduction for qualified investments and limitations on the deductibility of interest expense and executive compensation. In December 2017, the SEC issued Staff Accounting Bulletin No. 118, Income Tax Accounting Implications of the Tax Cuts and Jobs Act (SAB 118), which allows companies to record provisional amounts during a measurement period not to extend more than one year beyond the Act enactment date. Since the TCJA was passed late in the fourth quarter of 2017, and ongoing guidance and accounting interpretation are expected during the year, the Company considers the accounting for deferred tax remeasurements, the impact of the transition of U.S. international taxation from a worldwide tax system to a territorial system and other provisions to be incomplete. There have been no material changes to the provisional adjustments disclosed in the Company's 2017 Form 10-K. The Company is continuing to evaluate the estimates used to record and disclose the effects of the Tax Act.

Effective January 1, 2018, the TCJA created a new requirement to include in U.S. income global intangible low-taxed income (GILTI) earned by controlled foreign corporations ("CFC"). The effect of GILTI, and the associated foreign tax credit, is to effectively create a minimum floor of taxation on CFC profits that must be included currently in the gross income of the CFCs' U.S. shareholder. Under U.S. GAAP, we are allowed to make an accounting policy choice of either (1) treating taxes due on future U.S. inclusions related to GILTI as a current-period expense when incurred (the "period cost method") or (2) factoring such amounts into a company's measurement of its deferred taxes (the "deferred method"). The Company uses the period cost method in recording the tax effects of GILTI in its financial statements.

The Company's income tax provision and effective tax rates for the three and six months ended June 29, 2018 were $2.9 million and 13.2% and $5.4 million and 11.0% and $3.1 million and 13.3% and $7.6 million and 18.0% for the three and six months ended June 30, 2017. The change in respective rates reflects, primarily, the recently enacted TCJA as discussed above, changes in the geographic mix of worldwide earnings and financial results in jurisdictions which are taxed at different rates, the impact of losses in jurisdictions with full federal and state valuation allowances and tax benefits associated with share-based compensation.

Company management continuously evaluates the need for a valuation allowance and, as of June 29, 2018, concluded that a full valuation allowance on its federal and state deferred tax assets as well as the deferred tax assets of one its Singapore subsidiaries was still appropriate.

The Company provides for U.S. income taxes on its undistributed earnings of foreign subsidiaries as required by the TCJA. However, the Company does not provide for any withholding taxes on its undistributed earnings of its subsidiaries that it intends to invest indefinitely outside the U.S. In prior years, the Company determined that a portion of the current year earnings of one of its China subsidiaries may be remitted in the future to one of its foreign subsidiaries outside of mainland China and, accordingly, the Company provided for the related withholding taxes in its condensed consolidated financial statements. The Company does not currently plan to remit any earnings from its China subsidiaries to any other foreign subsidiary in 2018. If the Company changes its intent to reinvest its undistributed foreign earnings indefinitely or if a greater amount of undistributed earnings are needed than the previous anticipated remaining unremitted foreign earnings, the Company could be required to accrue or pay foreign taxes on some or all of these undistributed earnings. As of June 29, 2018, the Company had undistributed earnings of foreign subsidiaries that are indefinitely invested outside of the U.S. of approximately $207.6 million. It is not practicable to determine the tax liability that might be incurred if these earnings were to be distributed.

The Company's gross liability for unrecognized tax benefits as of June 29, 2018 and June 30, 2017 was $0.3 million and $0.3 million, respectively. Although it is possible some of the unrecognized tax benefits could be settled within the next twelve months, the Company cannot reasonably estimate the outcome at this time.

8. Net Income Per Share

Basic net income per share excludes dilution and is computed by dividing net income by the weighted average number of common shares outstanding for the period. Diluted net income per share reflects the potential dilution that would occur if outstanding securities or other contracts to issue common stock were exercised or converted into common

stock.

The following is a reconciliation of the numerators and denominators used in computing basic and diluted net income (loss) per share (in thousands, except per share data):

	Three Months Ended		Six Months Ended	
	June 29, 2018	June 30, 2017	June 29, 2018	June 30, 2017
Numerator:				
Net income	$18,960	$20,179	$43,701	$34,520
Denominator:				
Shares used in computation — basic:				
Weighted average common shares outstanding	38,802	33,433	37,763	33,247
Shares used in computation — diluted:				
Shares used in computing basic net income per share	38,802	33,433	37,763	33,247
Dilutive effect of common shares outstanding subject to repurchase	489	622	649	749
Dilutive effect of options outstanding	6	9	6	21
Weighted average shares used in computing diluted net income per share	39,297	34,064	38,418	34,017
Net income per share — basic	$0.49	$0.60	$1.16	$1.04
Net income per share — diluted	$0.48	$0.59	$1.14	$1.01

On February 2, 2018, the Company successfully completed a follow-on offering whereby the Company issued 4,761,905 shares of its common stock. The weighted average impact for the six months ended June 29, 2018 was 3,872,318 shares.

9. Commitments and Contingencies

The Company had commitments to purchase inventory totaling approximately $134.2 million at June 29, 2018.

The Company leases properties domestically in Hayward, California, Austin, Texas, Chandler, Arizona and South San Francisco, California and internationally in China, Singapore, the Philippines and the Czech Republic. The Company leases certain of its facilities under non-cancelable leases, which expire on various dates through 2023.

As of June 29, 2018, future minimum payments under these operating leases were as follows (in thousands):

Fiscal Year	
2018 (remaining in year)	$4,110
2019	6,256
2020	5,250

2021	4,640
2022	3,840
Thereafter	116
Total minimum lease payments	$24,212

From time to time, the Company is subject to various legal proceedings and claims, either asserted or unasserted, that arise in the ordinary course of business. Although the outcome of the various legal proceedings and claims cannot be predicted with certainty, the Company has not had a history of outcomes to date that have been material to the statement of operations and does not believe that any of these proceedings or other claims will have a material adverse effect on its consolidated financial condition or results of operations.

10. Geographical Information

The Company's principal markets include North America, Asia and Europe. The Company's foreign operations are conducted primarily through its wholly-owned subsidiaries in China, Singapore and the Czech Republic. Sales by geographic area represent sales to unaffiliated customers and are based upon the location to which the products were shipped. The following table sets forth revenue by geographic area (in thousands):

	Three Months Ended		Six Months Ended	
	June 29, 2018	June 30, 2017	June 29, 2018	June 30, 2017
United States	$159,187	$129,349	$343,962	$233,705
China	16,812	5,166	18,978	18,113
Singapore	82,904	73,810	185,537	134,050
Austria	16,393	8,491	29,929	19,712
Other	14,917	11,445	26,649	27,275
	$290,213	$228,261	$605,055	$432,855

At June 29, 2018, approximately $10.0 million and $1.5 million of the Company's net long-lived assets were located in Asia and the Czech Republic, respectively, and the remaining balances were located in the United States. At June 30, 2017, approximately $6.5 million and $1.6 million of the Company's net long-lived assets were located in Asia and the Czech Republic, respectively, and the remaining balances were located in the United States.

11. Subsequent Events

On July 24, 2018, the Company entered into an Agreement and Plan of Merger (the "Merger Agreement") to acquire Quantum Global Technologies, LLC ("Quantum"), for approximately $342.0 million in cash, subject to certain closing adjustments as provided in the Merger Agreement, including a working capital adjustment, and up to $15.0 million of potential cash earn-out payments if Quantum achieves certain specified revenue levels through December 27, 2019, pursuant to the provisions of the Merger Agreement. The Company's primary reason for this acquisition is to expand UCT into an adjacent market and increase the served addressable market in its core semiconductor business.

The Company also entered into a commitment letter (the "Commitment Letter") with Barclays Bank PLC ("Barclays"), pursuant to which Barclays has committed to provide senior secured credit facilities to the Company in an aggregate amount of $400.0 million, comprised of (i) $350.0 million under a seven-year senior secured term loan B facility (the "Term Loan") and (ii) $50.0 million under a five-year senior secured revolving credit facility (the "Revolving Credit Facility" and, together with the Term Loan, the "Credit Facilities"). The Term Loan, together with cash on hand, will be used to finance the transaction contemplated by the Merger Agreement, refinance existing debt, and pay fees and expenses incurred in connection with the Credit Facilities and the acquisition. The Revolving Credit Facility will be used to provide ongoing working capital and capital for other general corporate purposes of the Company and its subsidiaries.

The Merger is expected to close in the third quarter of 2018, and is subject to customary regulatory approvals and closing conditions, including the expiration or termination of the waiting period under the Hart-Scott- Rodino Act. Barclays' commitment to provide the Credit Facilities is subject to customary closing conditions.

ITEM 2. Management's Discussion And Analysis of Financial Condition And Results Of Operations

You should read the following discussion of our financial condition and results of operations in conjunction with the condensed consolidated financial statements and the notes thereto included elsewhere in this Quarterly Report on Form 10-Q and in our Annual Report on Form 10-K filed with the SEC on March 14, 2018. This Quarterly Report on Form 10-Q contains "forward-looking statements" that involve substantial risks and uncertainties. The statements contained in this Quarterly Report on Form 10-Q that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act, and Section 21E of the Securities Exchange Act of 1934, as amended, including, but not limited to, statements regarding our expectations, beliefs, intentions, strategies, future operations, future financial position, future revenue, projected expenses, gross margins and plans and objectives of management. In some cases, you can identify forward-looking statements by terms such as "anticipate," "believe," "estimate," "expect," "intend," "may," "might," "plan," "project," "will," "would," "should," "could," "can," "predict," "poten "objective," or the negative of these terms, and similar expressions intended to identify forward-looking statements. However, not all forward-looking statements contain these identifying words. These forward-looking statements reflect our current views about future events and involve known risks, uncertainties and other factors that may cause our actual results, performance or achievement to be materially different from those expressed or implied by the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those identified below, and those discussed in the section titled "Risk Factors" included in this Quarterly Report on Form 10-Q and in our Annual Report on Form 10-K filed with the SEC on March 14, 2018. Furthermore, such forward-looking statements speak only as of the date of this report. Except as required by law, we undertake no obligation to update any forward-looking statements to reflect events or circumstances after the date of such statements.

Overview

We are a global leader in the design, engineering, and manufacture of production tools, modules and subsystems for the semiconductor capital equipment industry and industry segments with similar requirements including display, consumer and medical. We focus on providing specialized engineering and manufacturing solutions for these applications. We enable our customers to realize lower manufacturing costs and reduced design-to-delivery cycle times while maintaining high quality standards.

We ship a majority of our products to U.S. registered customers with locations both in and outside the U.S. In addition to U.S. manufacturing, we manufacture products in our Asian facilities to support local and U.S. based customers. We conduct our operating activities primarily through our wholly owned subsidiaries, Ultra Clean Technology Systems and Service, Inc., AIT, Ultra Clean Micro-Electronics Equipment (Shanghai) Co., Ltd., Ultra Clean Asia Pacific, Pte, Ltd., Thermal and FDS.

Financial Highlights and Market Trends

We believe our ability to custom design, manufacture, and deliver on unexpected, time-sensitive orders, as well as our commitment to customer satisfaction, continues to strengthen our position as a critical supplier to our customers. Our ability to provide engineering, critical fabrication, integration and testing capabilities on short notice, while meeting stringent quality levels, has made us a preferred outsourcing partner in the semiconductor capital equipment industry. Healthy demand drivers supporting the WFE market positions us to take advantage of continued opportunities in the semiconductor market over the long-term. We also continue to actively consider ways to broaden our capabilities and offerings for our customers, both organically and through strategic acquisitions, and actively focus on driving operational efficiencies to adjust to market conditions.

We believe the overall semiconductor market will see sustained long-term strength from ongoing demand caused by a broad range of drivers, including emerging application such as autonomous vehicles, the Internet of Things, high

performance computing, artificial intelligence, and technology to support the data sharing economy. We also believe that semiconductor equipment OEMs are increasingly relying on partners like UCT to fulfill their expanding capacity requirements. Midway through 2018, we began to see a reduction in orders from some of our OEM customers, as certain manufacturers announced they were deferring capital investment. We expect the impact of these reductions to be reflected beginning in the third quarter of 2018.

We have in the past made acquisitions of complementary businesses and assets and regularly evaluate opportunities to acquire complementary businesses or assets. On July 24, 2018, the Company entered into an Agreement and Plan of Merger (the “Merger Agreement”) to acquire Quantum Global Technologies, LLC (“Quantum”) for approximately $342.0 million in cash, subject to certain closing adjustments as provided in the Merger Agreement, including a working capital adjustment, and up to $15.0 million of potential cash earn-out payments if Quantum achieves certain specified revenue levels through December 27, 2019, pursuant to the provisions of the Merger Agreement. The Company’s primary reason for this acquisition is to expand UCT into an adjacent market and increase the served addressable market in its core semiconductor business.

The Company also entered into a commitment letter (the "Commitment Letter") with Barclays Bank PLC ("Barclays"), pursuant to which Barclays has committed to provide senior secured credit facilities to the Company in an aggregate amount of $400.0 million, comprised of (i) $350.0 million under a seven-year senior secured term loan B facility (the "Term Loan") and (ii) $50.0 million under a five-year senior secured revolving credit facility (the "Revolving Credit Facility" and, together with the Term Loan, the "Credit Facilities"). The Term Loan, together with cash on hand, will be used to finance the transaction contemplated by the Merger Agreement, refinance existing debt, and pay fees and expenses incurred in connection with the Credit Facilities and the acquisition. The Revolving Credit Facility will be used to provide ongoing working capital and capital for other general corporate purposes of the Company and its subsidiaries.

The Merger is expected to close in the third quarter of 2018, and is subject to customary regulatory approvals and closing conditions, including the expiration or termination of the waiting period under the Hart-Scott- Rodino Act. Barclays' commitment to provide the Credit Facilities is subject to customary closing conditions.

Results of Operations

For the periods indicated, the following table sets forth certain costs and expenses and other income items as a percentage of sales. The table and subsequent discussion should be read in conjunction with our Condensed Consolidated Financial Statements and Notes thereto included elsewhere in our quarterly report.

	Three Months Ended		Six Months Ended	
	June 29, 2018	June 30, 2017	June 29, 2018	June 30, 2017
Sales	100.0 %	100.0 %	100.0 %	100.0 %
Cost of goods sold	84.1 %	81.0 %	84.3 %	81.3 %
Gross profit	15.9 %	19.0 %	15.7 %	18.7 %
Operating expenses:				
Research and development	1.0 %	1.2 %	1.0 %	1.3 %
Sales and marketing	1.3 %	1.5 %	1.2 %	1.5 %
General and administrative	5.8 %	5.6 %	5.3 %	5.6 %
Total operating expenses	8.1 %	8.3 %	7.5 %	8.4 %
Income from operations	7.8 %	10.7 %	8.2 %	10.3 %
Interest and other income (expense), net	(0.3)%	(0.5)%	(0.1)%	(0.5)%
Income before provision for income taxes	7.5 %	10.2 %	8.1 %	9.8 %
Income tax provision	1.0 %	1.4 %	0.9 %	1.8 %
Net income	6.5 %	8.8 %	7.2 %	8.0 %

Sales

Sales for the three months ended June 29, 2018 were $290.2 million, an increase of $61.9 million, or 27.1%, from $228.3 million in the comparable quarter of 2017. The increase in overall sales in the second quarter of 2018 compared to the second quarter of 2017 is primarily due to an increase in demand from our existing semiconductor customers as a result of generally strong demand in the semiconductor industry during the period. On a geographic basis, sales in the U.S. increased $10.8 million to $120.5 million, or 41.5% of sales, for the three months ended June 29, 2018 compared to $109.7 million, or 48.1% of sales, for the comparable period of 2017. Foreign sales

increased $51.1 million to $169.7 million, or 58.5% of sales, for the three months ended June 29, 2018 compared to $118.6 million, or 51.9% of sales, for the comparable period of 2017.

Sales for the six months ended June 29, 2018, were $605.1 million, an increase of $172.2 million, or 39.8%, from $432.9 million in the comparable period of 2017. The increase in sales for the six months ended June 29, 2018, which includes increases of $170.7 million and $1.5 million in semiconductor and non-semiconductor industries, respectively, was due to an increase in the volume of products shipped as a result of continued semiconductor demand from our major customers. Sales in the U.S. for the six months ended June 29, 2018 increased by $46.0 million to $254.5 million while foreign sales increased by $126.2 million to $350.6 million when compared to the same period in prior year.

We expect sales to be lower in the third quarter of fiscal 2018 due to forecasted weaker demand in the semiconductor industry.

Gross Profit

Cost of goods sold consists primarily of purchased materials, labor and overhead, including depreciation related to certain capital assets associated with the design and manufacture of products sold.

Gross profit for the three months ended June 29, 2018 increased $2.7 million to $46.1 million, or 15.9% of sales, from $43.4 million, or 19.0% of sales, for the three months ended June 30, 2017. Gross profit for the six months ended June 29, 2018, increased by $14.0 million to $94.9 million, or 15.7% of sales, from $80.9 million, or 18.7% of sales, for the six months ended June 30, 2017.

The increase in gross profit dollars for the three and six months ended June 29, 2018 compared to the same periods in 2017 was primarily due to higher volume of products shipped. The decrease in gross margin in the three and six months ended June 29, 2018 compared to the same periods in 2017 was due mostly to a change in product mix with higher costs required to meet higher customer demand during fiscal 2018, as well as due to an accelerated ramp of new products, offset partially by an increase in labor efficiency.

We expect gross profit to decrease in the third quarter of 2018 as compared to the second quarter of 2018 due to the expected decrease in revenues for the third quarter of 2018 as described above.

Research and Development Expense

Research and development expense consists primarily of activities related to new component testing and evaluation, test equipment and fixture development, product design, and other product development activities. Research and development expense for the three months ended June 29, 2018 increased $0.1 million, or 5.1%, to $2.9 million, or 1.0% of sales, compared to $2.8 million, or 1.2% of sales in the comparable period in 2017.

Research and development expense for the six months ended June 29, 2018 increased by $0.2 million, or 4.6%, to $5.9 million, or 1.0% of sales, compared to $5.7 million, or 1.3% of sales in the comparable period in 2017.

The increase in research and development expense when comparing the three and six months ended June 29, 2018 with the comparable periods in 2017 was due to an increase in non-production related engineering work and an increase in employee incentive compensation related expenses as a result of higher profitability.

Sales and Marketing Expense

Sales and marketing expense consists primarily of salaries and commissions paid to our sales and service employees, salaries paid to our engineers who work with the sales and service employees to help determine the components and configuration requirements for new products and other costs related to the sales of our products. Sales and marketing expense for the three months ended June 29, 2018 increased $0.2 million, or 8.3 %, to $3.6 million, or 1.3% of sales, compared to $3.4 million, or 1.5% of sales, in the comparable period of 2017. Sales and marketing expense for the six months ended June 29, 2018 increased by $1.0 million, or 16.1%, to $7.4 million, or 1.2% of sales, compared to $6.4 million, or 1.5% of sales in the comparable period in 2017.

The increase in sales and marketing expenses when comparing the three and six months ended June 29, 2018 with the comparable period in 2017 was due to an increase in employee incentive compensation related expenses as a result of increase in employee headcount and higher profitability.

General and Administrative Expense

Our general and administrative expense has historically consisted primarily of salaries and overhead associated with our administrative staff, professional fees and amortization of our intangible assets. General and administrative expense increased $4.1 million, or 31.3%, for the three months ended June 29, 2018, to $16.9 million, or 5.8% of sales, compared with $12.8 million, or 5.6% of sales, in the comparable period of 2017. General and administrative expense increased approximately $7.3 million, or 29.7%, for the six months ended June 29, 2018, to $31.9 million, or 5.3% of sales, compared with $24.6 million, or 5.6% of sales, in the comparable period of 2017.

The increase in general and administrative expenses when comparing the three and six months ended June 29, 2018 with the comparable periods in 2017 was primarily due to an increase in outside services resulting from the non-capitalizeable implementation costs of our new enterprise reporting system, higher employee incentive compensation related expenses as a result of an increase in headcount, higher operating income and severance pay associated with the departure of an officer from the Company.

Interest and Other Income (Expense), net

Interest and other income (expense), net, for the three and six months ended June 29, 2018, was $(0.8) million and $(0.5) million, respectively, compared to $(1.1) million and $(2.1) million, respectively, in the comparable periods of 2017. The decrease in net expense for the three and six months ended June 29, 2018 compared to the same periods in the prior year was primarily due to an increase in the fair value of the Company’s non-designated derivative financial instruments and to a decrease in interest expense as a result of a lower principal balance on our debt.