

DESWELL INDUSTRIES INC  
Form 20-F  
July 14, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

(Mark one)

REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR (g) OF THE SECURITIES EXCHANGE ACT OF 1934

OR

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

For the fiscal year ended March 31, 2017

OR

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

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

OR

o SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

Date of event requiring this shell company report

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

Commission File Number: 001-33900

**DESWELL INDUSTRIES, INC.**

(Exact name of registrant as specified in its charter)

British Virgin Islands  
(Jurisdiction of incorporation or organization)

10B, Edificio Associacao Industrial De Macau  
32 Rua do Comandante Mata e Oliveira, Macao  
Special Administrative Region, PRC  
(Address of Principal Executive Offices)

Herman Wong, Chief Financial Officer,  
Telephone: 853-28-322096; fax: 853-28-323265  
E-mail: hermanwong@jetcrown.net

10B, Edificio Associacao Industrial De Macau  
32 Rua do Comandante Mata e Oliveira, Macao  
Special Administrative Region, PRC

(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person)

Securities registered or to be registered pursuant to Section 12(b) of the Act: Common shares, no par value

Securities registered or to be registered pursuant to Section 12(g) of the Act: NONE

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: NONE

Edgar Filing: DESWELL INDUSTRIES INC - Form 20-F

As of March 31, 2017, there were 15,885,239 common shares of the registrant outstanding.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  
 Yes  No

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  Yes  No

Note – Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

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, or a non-accelerated filer. See definition of “accelerated filer and large accelerated filer” in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated  Accelerated filer  Non-accelerated filer

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP  International Financial Reporting Standards as issued by the International Accounting Standards Board   
 Other

If “Other” has been checked, indicate by check mark which financial statement item the registrant has elected to follow:  
Item 17  Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  Yes  No

## TABLE OF CONTENTS

Page		
	INTRODUCTION	3
	FINANCIAL STATEMENTS AND CURRENCY PRESENTATION	3
	PART I	3
Item 1.	IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS	3
Item 2.	OFFER STATISTICS AND EXPECTED TIMETABLE	3
Item 3.	KEY INFORMATION	3
Item 4.	INFORMATION ON THE COMPANY	20
Item 4A.	UNRESOLVED STAFF COMMENTS	30
Item 5.	OPERATING AND FINANCIAL REVIEW AND PROSPECTS	30
Item 6.	DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES	40
Item 7.	MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS	43
Item 8.	FINANCIAL INFORMATION	44
Item 9.	THE OFFER AND LISTING	45
Item 10.	ADDITIONAL INFORMATION	46
Item 11.	QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK	53
Item 12.	DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES	54
	PART II	54
Item 13.	DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES	54
Item 14.	MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS	54
Item 15.	CONTROLS AND PROCEDURES	54
Item 16.	[RESERVED]	55
Item 16A.	AUDIT COMMITTEE FINANCIAL EXPERT	55
Item 16B.	CODE OF ETHICS	55
Item 16C.	PRINCIPAL ACCOUNTANT FEES AND SERVICES	55
Item 16D.	EXEMPTIONS FROM THE LISTING STANDARDS FOR THE AUDIT COMMITTEE.	56
Item 16E.	PURCHASES OF EQUITY SECURITIES BY THE ISSUER AND AFFILIATE PURCHASERS	56
Item 16F.	CHANGE IN REGISTRANT'S CERTIFYING ACCOUNTANT	57
Item 16G.	CORPORATE GOVERNANCE	57
Item 16H.	MINE SAFETY DISCLOSURE	57
	PART III	57
Item 17.	FINANCIAL STATEMENTS	57
Item 18.	FINANCIAL STATEMENTS	57

Item 19. EXHIBITS	57
SIGNATURES	58
	59
CERTIFICATION OF CHIEF EXECUTIVE OFFICER REQUIRED BY RULE 13a-14(a) OR RULE 15d-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934	Exhibit 12.1
CERTIFICATION OF CHIEF FINANCIAL OFFICER REQUIRED BY RULE 13a-14(a) OR RULE 15d-14(a) UNDER THE SECURITIES EXCHANGE ACT OF 1934	Exhibit 12.2
CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002	Exhibit 13.1
CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM — BDO China Shu Lun Pan Certified Public Accountants LLP	Exhibit 15.1

## INTRODUCTION

This Annual Report on Form 20-F contains forward-looking statements. These statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those anticipated in the forward-looking statements. Factors that might cause such a difference include, but are not limited to those discussed in the section entitled Risk Factors under Item 3 “Key Information.”

Readers should not place undue reliance on forward-looking statements, which reflect management’s view only as of the date of this Annual Report. The Company undertakes no obligation to revise these forward-looking statements to reflect subsequent events or circumstances. Readers should also carefully review the risk factors described in other documents the Company files from time to time with the Securities and Exchange Commission.

Except where the context otherwise requires and for purposes of this Report only:

- “we,” “us,” “our company,” “our,” the “Company” or “Deswell” refers to Deswell Industries, Inc. and, in the context of describing our operations, also include our operating subsidiaries;
- “shares” refer to our common shares, no par value;
- “China” or “PRC” refers to the People’s Republic of China, excluding Taiwan, Hong Kong and Macao;
- “Hong Kong” refers to the Hong Kong Special Administrative Region of the People’s Republic of China;
- “Macao” refers to the Macao Special Administrative Region of the People’s Republic of China;
- “BVI” refers to the British Virgin Islands;
- all references to:
  - o renminbi, “RMB” or yuan are to the legal currency of China, of which the yuan is the base unit;
  - o “HK dollars” or “HK\$” are to the legal currency of Hong Kong;
  - o “MOP\$” are to the legal currency of Macao;
  - o “U.S. dollars,” “dollars,” “\$” or “U.S.\$” are to the legal currency of the United States; and
  - o “fiscal year,” e.g., “fiscal 2017,” are to our year ended March 31 of the year(s) indicated.

## FINANCIAL STATEMENTS AND CURRENCY PRESENTATION

The Company prepares its consolidated financial statements in accordance with generally accepted accounting principles in the United States of America and publishes such statements in United States dollars. See “Report of Independent Registered Public Accounting Firm” included elsewhere herein. The Company publishes its financial statements in United States dollars. The functional currency of the Company and its subsidiaries is the U.S. dollar.

### PART I

#### **Item 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS**

Not applicable.

#### **Item 2. OFFER STATISTICS AND EXPECTED TIMETABLE**

Not applicable.

#### **Item 3. KEY INFORMATION**

The selected financial data set forth below should be read in conjunction with our Consolidated Financial Statements and Notes thereto included at page 57 of this Annual Report. The selected Operations Data for each



of the three fiscal years in the period ended March 31, 2017, and the Balance Sheet data as of March 31, 2016 and 2017 are derived from our audited Consolidated Financial Statements included in this Annual Report. The selected Operations Data for the years ended March 31, 2013 and 2014, and the Balance Sheet data as of March 31, 2013, 2014, and 2015 are derived from our audited Consolidated Financial Statements, which are not included in this Annual Report.

### Selected Financial Data <sup>(1)</sup>

(in thousands except per share and statistical data)

#### Consolidated Statement of Operations Data:

	Year ended March 31,				
	2013	2014	2015	2016	2017
Net sales	\$53,382	\$40,932	\$38,076	\$44,568	\$44,522
Cost of sales	46,171	37,295	33,852	39,775	37,073
Gross profit	7,211	3,637	4,224	4,793	7,449
Selling, general and administrative expenses	10,714	10,257	9,123	9,119	8,856
Other income (expenses), net	233	(214 )	93	(1,021 )	(696 )
Operating loss	(3,270 )	(6,834 )	(4,806 )	(5,347 )	(2,103 )
Non-operating income, net	2,056	379	2,553	571	3,688
(Loss) income before income taxes	(1,214 )	(6,455 )	(2,253 )	(4,776 )	1,585
Income taxes	328	624	207	158	209
(Loss) income from continuing operations, after income taxes	(1,542 )	(7,079 )	(2,460 )	(4,934 )	1,376
Loss from discontinued operations, net of tax	(449 )	(411 )	(348 )	—	—
Net (loss) income attributable to Deswell Industries, Inc.	(1,991 )	(7,490 )	(2,808 )	(4,934 )	1,376
Other comprehensive income (loss):					
Unrealized gain (loss) on available-for-sale securities <sup>(2)</sup>	718	57	33	(73 )	(3 )
Reclassification adjustment in connection with loss on disposal of available-for-sale securities transferred to profit or loss.	—	—	—	—	14
Total comprehensive (loss) income attributable to Deswell Industries, Inc.	\$(1,273 )	\$(7,433 )	\$(2,775 )	\$(5,007 )	\$1,387
Net (loss) income per share attributable to Deswell Industries, Inc.:					
Basic and Diluted:					
(Loss) income from continuing operations per share <sup>(3)</sup>	\$(0.09 )	\$(0.43 )	\$(0.15 )	\$(0.31 )	\$0.09
Loss from discontinued operations per share <sup>(3)</sup>	\$(0.03 )	\$(0.03 )	\$(0.02 )	\$—	\$—
	\$(0.12 )	\$(0.46 )	\$(0.17 )	\$(0.31 )	\$0.09
Weighted average common shares outstanding <sup>(3)</sup> (shares in thousands)	16,467	16,186	16,056	16,056	16,035
Statistical Data:					
Gross margin from continuing operations	13.5 %	8.9 %	11.1 %	10.8 %	16.7 %

Operating margin from continuing operations	(6.1 %)	(16.7 %)	(12.6 %)	(12.0 %)	(4.7 %)
---	---------	----------	----------	----------	---------

Dividends per share	\$0.30	\$0.22	\$0.19	\$0.14	\$0.105
---------------------	--------	--------	--------	--------	---------

## Balance Sheet Data:

	2013	2014	2015	2016	2017
Working capital	\$58,298	\$50,868	\$45,864	\$39,890	\$41,307
Total assets	112,565	100,636	96,439	87,571	90,987
Long-term debt, less current portion	—	—	—	—	—
Total debt	—	—	—	—	—
Shareholders' equity	101,576	89,610	84,063	76,808	76,201

(1) Our consolidated financial statements are prepared in accordance with generally accepted accounting principles in the United States of America and are stated in U.S. dollars. See “Financial Statements and Currency Presentation.”

(2) See Note 4 of Notes to Consolidated Financial Statements included later in this Report regarding unrealized gain (loss) on available-for-sale securities during the years ended March 31, 2016 and 2017.

(3) Basic loss per share excludes dilution from potential common shares and is computed by dividing loss attributable to Deswell shareholders by the weighted-average number of common shares outstanding for the period. Diluted loss per share reflects the potential dilution from potential common shares.

## Risk Factors

We may from time to time make written or oral forward-looking statements. Written forward-looking statements may appear in this document and other documents filed with the Securities and Exchange Commission, in press releases, in reports to shareholders, on our website, and other documents. The Private Securities Litigation Reform Act of 1995 contains a safe harbor for forward-looking statements on which we rely in making such disclosures. In connection with this “safe harbor,” we are hereby identifying important factors that could cause actual results to differ materially from those contained in any forward-looking statements made by us or on our behalf. Any such statement is qualified by reference to the following cautionary statements:

We are, and have been, dependent on a few major customers, the loss of, or substantial reduction in orders from, which would substantially harm our business and operating results.

Historically, we have depended, currently depend, and expect to continue to depend, on a small number of customers for a significant percentage of our net sales. During the year ended March 31, 2017, we had three major customers, each accounting for more than 10% of our net sales and together for 33.6% of our net sales. If our major customers experience a decline in the demand for their products as a result of the prevailing economic environment or other

factors, the products or services that we provide to them could be reduced or even terminated. The loss of any of our major customers or a substantial reduction in orders from any of them would adversely impact our sales and operating results unless and until we were able to increase sales from other existing customers or add sales from new customers.

Our sales are based on purchase orders and we have no long-term contracts with any of our customers and the percentage of sales to any of our customers has fluctuated in the past and may fluctuate in future. We cannot assure you that present or future customers will not cease using us as the source of the injection-molded plastic parts and components we manufacture, for electronic manufacturing services of electrical products and subassemblies or significantly change, reduce or delay the amount of products and services ordered from us.

Uncertainty and adverse changes in the economy and financial markets have had, and could continue to have, an adverse impact on our business and operating results.

As a result of the recent global economic downturn, many businesses, including those of several of our customers, experienced weaker demand for their products and services. Our customers so affected, in turn, were more conservative in ordering our products and services. There are continuing concerns over price instability, geopolitical issues, availability and cost of credit, stability of financial markets and sovereign nations. Uncertainty or adverse changes in the economy could negatively impact:

- the demand for our customers' products,
- the amount, timing and stability of their orders to us,

5

- the financial strength of our customers and suppliers,
- our customers' and suppliers' ability or willingness to do business with us,
- our suppliers' and customers' ability to fulfill their obligations to us,
- the ability of our customers, our suppliers or us to obtain credit, secure funds or raise capital, or
- the prices at which we can sell our products and services,

which, in turn, could adversely affect

- our ability to manage inventory levels effectively or collect receivables,
- our cash flow position,
- our net sales, gross margins and operating results; or
- otherwise adversely impact our results of operations, financial condition and liquidity.

Our gross margins fluctuate from year to year and may be adversely affected by a number of factors.

The following chart shows, for the years indicated, our gross margins from our two principal operating segments and for our company as a whole:

#### Gross Margins Percentage

We expect gross margins generally and for specific products to continue to fluctuate from year to year. Fluctuations in our margins have been affected, often adversely, and may continue to be affected, by numerous factors, including:

- our cost of raw materials, especially our cost of electronic components due to changes in the prices, availability and long lead time of components and parts needed for the manufacturing of electronic products;
- costs of labor, particularly in recent years, when such costs have increased substantially as a consequence of increasing governmental regulation directed at labor practices and policies;

6

the appreciation of the exchange rate of the RMB, in which we pay our labor and manufacturing costs, against the U.S. dollar, in which we present our financial statements;

- changes in our customer mix or the mix of higher and lower margin products, or a combination of both in any year;
- price increases for products which, for competitive reasons, we choose to allow as concessions in an effort to maintain our customer base;
- increases in value-added taxes as result of changes in the value-added tax policy of the Chinese government for various categories of export products; and
- increased costs to conform our products to consumer and product safety laws and regulations of the various countries in which our products are sold.

If we cannot maintain stability in our gross margins, our operating results could suffer, dividend payments to shareholders may be decreased or eliminated, our financial position may be harmed and our stock price may fall.

We believe we were a passive foreign investment company, or “PFIC,” for our fiscal year ended March 31, 2017 under U.S. income tax laws and may be a PFIC for years after fiscal 2017. If we were a PFIC in fiscal 2017, or are a PFIC in later years, U.S. investors could suffer adverse U.S. federal income tax consequences in such years.

The determination of whether we are a passive foreign investment company, or PFIC, in any taxable year is made on an annual basis after the close of that year and depends on the composition of our income and the nature and value of our assets, including goodwill. Specifically, we will be classified as a PFIC if, after applying relevant look-through rules with respect to the income and assets of subsidiaries, either (i) 75% or more of our gross income for such taxable year is passive income, or (ii) 50% or more of the value of our assets (based on an average of the quarterly values of the assets during such year) is attributable to assets that either produce passive income or are held for the production of passive income (the “PFIC asset test”). Cash and cash equivalents, even if they are part of the working capital of a company, constitute “passive” assets for the purposes of the PFIC asset test.

We believe that we were a PFIC for our year ended on March 31, 2017 and may also be a PFIC in subsequent tax years. If we are a PFIC for any year during a U.S. Holder’s holding period of our common shares, then such U.S. Holder generally could be subject to adverse U.S. tax consequences including the requirement to treat any “excess distribution” received on our common shares, or any gain realized upon a disposition of such common shares, as ordinary income and to pay an interest charge on a portion of such distributions or gain.

Because of the complexity of the issues regarding our classification as a PFIC, U.S. investors are urged to consult their own tax advisors for guidance as to our PFIC status. For further discussion of the adverse U.S. federal income tax consequences arising from the classification as a PFIC, please see “United States Federal Income Tax – Passive Foreign Investment Company (PFIC)” in ITEM 10 Additional Information beginning on page 50 of this Report.

The economy of China has been experiencing significant growth, leading to inflation and increased labor costs. Increases in labor costs of workers in the PRC generally, and in the Province where our manufacturing facilities are

located particularly, have had and can be expected to continue to have a material and adverse effect on our operating results.

We generate all revenues from sales of products that we manufacture at our facilities located in Dongguan, Guangdong Province, in the PRC. The economy in China has grown significantly over the past 20 years, which has resulted in an increased inflation and the average cost of labor.

The inflation rate in China rose 1.5% year-on-year in May of 2017. However, the Company's actual cost of operations has significantly exceeded the overall inflation rate in China. The rapid growth of China's economy in general has in the past few years increased the Company's operating costs, including energy prices and labor costs. These increased costs have adversely affected the Company's cost of operations, caused the Company to increase its prices, and resulted in the loss of some customers.

There is no fixed minimum wage which is applicable to all of China; local governments in China adopt different amounts based on the situation in their area. China's Guangdong Province, where our manufacturing facilities are located, raised minimum wages by approximately 20% May 2011 and another 19.1% in March 2013.

Effective May 1, 2015, minimum wage levels across Guangdong Province, including Dongguan, where our manufacturing facilities are located, were increased by an average of 15.3%. Since May 1, 2015, there have been no adjustments made to the minimum wage in Guangdong Province.

In China, regional governments are authorized to set their own minimum wages according to local conditions. Increases in wages also result in increases in our and other employer's contributions for various mandatory social welfare benefits for Chinese employees that are based on percentages of their salaries. Continuing material increases in our cost of labor will continue to increase our operating costs and will adversely affect our financial results unless we pass on such increases to our customers by increasing the prices of our products and services. The effect of increases in the prices of our products and services would make our products more expensive in global markets, such as the United States and the European Union. This could result in the loss of customers, who may seek, and be able to obtain, products and services comparable to those we offer in lower-cost regions of the world. If we do not increase our prices to pass on the effect of increases in our labor costs, our margins and financial results would suffer.

Because most of our labor costs are incurred in China and therefore paid in RMB, the adverse effect on our business and financial results from increasing labor costs has historically been exacerbated by the appreciation in the exchange rate to the U.S. dollar, as is discussed in the next risk factor.

Changes in currency exchange rates have and could continue to influence our financial results significantly.

Our sales are mainly in United States dollars and Hong Kong dollars and our expenses are mainly in United States dollars, Hong Kong dollars and Chinese RMB.

The Hong Kong dollar has been pegged to the U.S. dollar at approximately 7.80 and has been relatively stable. The Hong Kong government may not continue to maintain the present currency exchange mechanism, which fixes the Hong Kong dollar at approximately 7.80 to each United States dollar and has not in the past presented a material currency exchange risk. Although announcements by Hong Kong's central bank indicate its intention to maintain the currency peg between the Hong Kong dollar and the U.S. dollar, if Hong Kong does change and follows China to a floating currency system or otherwise changes the exchange rate system of Hong Kong dollars to U.S. dollars, our margins and financial results could be adversely affected.

Between 1994 and July 2005, the market and official RMB rates were unified and the value of the RMB was essentially pegged to the U.S. dollar and was relatively stable. On July 21, 2005, the People's Bank of China adjusted the exchange rate of RMB to the U.S. dollar by linking the RMB to a basket of currencies and simultaneously setting the exchange rate of RMB to U.S. dollars, from 1:8.27, to a narrow band of around 1:8.11.



The chart below illustrates the fluctuations since the July 31, 2005 adjustment of the RMB to the U.S. dollar by showing the exchange ratio at the end of each of Deswell's fiscal years from March 31, 2006 to March 31, 2017. Because most of the Company's labor costs are incurred in China and therefore paid in RMB, the adverse effect on Deswell's business and financial results from increasing labor costs has in previous years been exacerbated by the appreciation in the exchange rate to the U.S. dollar. However, in fiscal 2017, the RMB depreciated relative to the U.S. dollar, with the exchange rate mitigating rather than exacerbating the increasing labor costs experienced by the Company.

(1) RMB (yuan) to U.S. dollar data presented in this chart are the midpoint rates on March 31 of the year indicated as reported by “Historical Exchange Rates” at <http://www.oanda.com/currency/historical-rates/>.

The appreciation and depreciation in the exchange ratio of the RMB to the U.S. dollar increases and decreases, respectively, our costs and expenses to the extent paid in RMB. Of all of the costs and expenses for the PRC entities, which accounted for 98.2% of the Company total, about 52.0%, 47.2%, and 48.9% were in RMB during the years ended March 31, 2015, 2016 and 2017, respectively.

The PRC government may adopt an even more flexible currency policy, which, if adopted, could result in appreciation of the exchange rate of the RMB to the U.S. dollar beyond the appreciation experienced under China’s current system.

If the RMB continues its appreciation to the U.S. dollar under China’s currency exchange system, our operating costs will continue to increase, and if China adopts a different or more flexible system of currency exchange resulting in greater appreciation of the RMB to the U.S. dollar, our operating costs could increase even more. In either event, such appreciation would adversely affect our financial results in a manner similar to the effects we have suffered, and may in the future suffer, as a consequence of our increasing labor costs.

For a discussion of the risks to our business from increases in our costs of labor, please see the risk factor immediately above entitled “The economy of China has been experiencing significant growth, leading to inflation and increased labor costs. Increases in labor costs of workers in the PRC generally, and in the Province where our manufacturing facilities are located particularly, have had and can be expected to continue to have a material and adverse effect on our operating results.”

If OEMs stop or reduce their manufacturing outsourcing, our business could suffer.

Our revenues depend on outsourcing by OEMs to us and to other contract manufacturers for which we manufacture end-products or parts and components. Current and prospective customers continuously evaluate our capabilities against other providers as well as against the merits of manufacturing products themselves. Our business would be adversely affected if OEMs decide to perform these functions internally. Similarly, we depend on new outsourcing opportunities to militate against lost revenues arising from the decline in demand for our customers’ products as a consequence of prevailing global economic conditions, and our business would be adversely affected if we are not successful in gaining additional business from these opportunities or if OEMs do not outsource additional

manufacturing business.

We could experience credit problems with our customers, which could adversely impact our operating results and financial condition and could adversely reduce our future revenues.

We manufacture and sell injection-molded plastic parts and components and provide manufacturing services for electrical products and subassemblies to companies and industries that have in the past, and may in the future, experience financial difficulty, particularly in light of recent conditions in the credit markets and the overall worldwide economy. For information on the concentration of our credit risk, see Note 19 of Notes to Consolidated Financial Statements included later in this Report.

If our customers experience financial difficulty, we could have problems recovering amounts owed to us from these customers, or demand for our products and services from these customers could decline. If one or more of our customers, particularly customers to which we have extended substantial credit and which have become material account debtors on our accounts receivables, were to become insolvent or otherwise were unable to pay for the products or services provided by us on a timely basis, or at all, our operating results and financial condition could be adversely affected. Such adverse effects could include one or more of the following:

- provision or increased provision for doubtful accounts,
- a charge for inventory write-offs,
- a reduction in revenue,
- decreases in cash, and
- increases in working capital requirements.

Because material amounts of our funds are held in banks where only limited protection on deposit accounts is required, the failure of any bank in which we deposit our funds could result in a loss of those funds to the extent exceeding the amounts protected and could, depending on the amount involved, affect our ability to continue in business.

At March 31, 2017, we had cash on hand of \$8.1 million, time deposits maturing over three months of \$5.4 million and time deposits maturing over twelve months of \$2.9 million, which were invested in short-term interest bearing investments at banks or other financial institutions. Of that amount, approximately \$1.9 million was held in banks and other financial institutions in Hong Kong, \$4.7 million in Macao and \$9.8 million in the PRC. The Hong Kong government provides deposit protection up to a maximum amount of HK\$500,000 (approximately U.S.\$64,400 based on the midpoint exchange rate for June 30, 2017 reported by “Historical Exchange Rates” at <http://www.oanda.com/currency/historical-rates/>) for each depositor in any individual bank in Hong Kong, and the Macao government provides deposit protection up to a maximum amount of MOP\$500,000 (approximately U.S.\$64,100 based on the midpoint exchange rate for June 30, 2017 reported by “Historical Exchange Rates” at <http://www.oanda.com/currency/historical-rates/>) for each depositor with any individual bank in Macao. We understand that in the event of a bank failure of a bank in the PRC, a PRC-government agency is to provide some, unspecified, protections of deposit accounts to individual depositors. After three interest rate hikes in 2011, there were recommendations in early 2012