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Knowles Corp  
Form 10-K  
February 25, 2015  
UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10-K

(Mark One)

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

For the fiscal year ended December 31, 2014.

or

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

For the transition period from to

Commission File Number: 001-36102

Knowles Corporation  
(Exact name of registrant as specified in its charter)

Delaware  
(State or other jurisdiction of incorporation or organization)

90-1002689  
(I.R.S. Employer Identification No.)

1151 Maplewood Drive  
Itasca, Illinois  
(Address of principal executive offices)

60143  
(Zip Code)

(630) 250-5100  
(Registrant's telephone number, including area code)  
Securities registered pursuant to Section 12(b) of the Act:

Title of each class  
Common Stock, par value \$0.01 per share

Name of each exchange on which registered  
New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

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

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes  No

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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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

(Do not check if smaller reporting company)

Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

The aggregate market value of the voting and non-voting common stock held by non-affiliates of the registrant as of the close of business on June 30, 2014 was \$2,614,095,909. The registrant's closing price as reported on the New York Stock Exchange-Composite Transactions for June 30, 2014 was \$30.74 per share. The number of outstanding shares of the registrant's common stock as of February 18, 2015 was 85,069,974.

DOCUMENTS INCORPORATED BY REFERENCE

Certain information contained in the registrant's Proxy Statement for its 2015 Annual Meeting of Stockholders is incorporated by reference into Part III hereof.

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PART I

ITEM 1. BUSINESS

Our Separation from Dover Corporation

On February 28, 2014, Knowles Corporation ("Knowles") became an independent, publicly-traded company as a result of the distribution by Dover Corporation ("Dover") of 100% of the outstanding common stock of Knowles to Dover's stockholders. Dover's Board of Directors approved the distribution of its shares of Knowles on February 6, 2014. Knowles' Registration Statement on Form 10 was declared effective by the U.S. Securities and Exchange Commission on February 10, 2014. On February 28, 2014, Dover's stockholders of record as of the close of business on February 19, 2014 ("record date") received one share of Knowles common stock for every two shares of Dover common stock held as of the record date. Knowles' common stock began trading "regular-way" under the ticker symbol "KN" on the New York Stock Exchange on March 3, 2014.

Unless the context otherwise requires, references in this Annual Report on Form 10-K to (i) "Knowles," the "Company," "we," "our" or "us" refer to Knowles Corporation and its consolidated subsidiaries, after giving effect to the spin-off of Knowles from Dover Corporation, (ii) "Former Parent" refer to Dover Corporation and (iii) the "Separation" or the "Distribution" refer to our spin-off from our Former Parent. Knowles was incorporated in Delaware on June 12, 2013 for the purpose of holding certain of Former Parent's communication technologies businesses in connection with the Separation. The address of our principal executive offices is 1151 Maplewood Drive, Itasca, Illinois 60143. Our telephone number is 630-250-5100.

Our Company

We are a market leader and global supplier of advanced micro-acoustic solutions and specialty components serving the mobile communications, consumer electronics, medical technology, military, aerospace and industrial markets. We have a leading position in micro-electro-mechanical systems ("MEMS") microphones, speakers and receivers which are used in smartphones, tablets and mobile handsets. We are also a leading manufacturer of transducers used in hearing aids and other medical devices and have a strong position in oscillators (timing devices) and capacitor components which enable various types of communication. Our focus on the customer, combined with unique technology, rigorous testing and global scale, helps to deliver innovative solutions and consistently dependable and precise products.

Our Strategy

Knowles is committed to growing market leadership in our current business segments and potentially expanding into attractive adjacent markets. This will be accomplished by guiding our research and development efforts towards opportunities that exhibit the greatest potential for optimal long-term returns and through the expansion of our technology platforms, while maintaining the highest product quality and operational excellence in the business. Inorganic growth may also be part of our strategy. We will measure our success through revenue growth, margin expansion, market share gains, stockholder return and stakeholder satisfaction.

Our Business Segments

We are organized into two reportable segments based on how management analyzes performance, allocates capital and makes strategic and operational decisions. These segments were determined in accordance with the Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 280-Segment Reporting and are comprised of (i) Mobile Consumer Electronics ("MCE") and (ii) Specialty Components ("SC"). The segments are

aligned around similar product applications serving our key end markets, to enhance focus on end market growth strategies.

MCE designs and manufactures innovative acoustic products, including microphones, speakers, receivers and integrated modules used in several applications that serve the handset, tablet and other consumer electronic markets. Locations include the corporate office in Itasca, Illinois; sales, support and engineering facilities in North America, Europe and Asia; and manufacturing facilities in Asia.

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SC specializes in the design and manufacture of specialized electronic components used in medical and life science applications, as well as high-performance solutions and components used in communications infrastructure and a wide variety of other markets. SC's transducer products are used principally in hearing aid applications within the commercial audiology markets, while its oscillator products predominantly serve the telecom infrastructure market and its capacitor products are used in applications including radio, radar, satellite, power supplies, transceivers and medical implants serving the defense, aerospace, telecommunication and life sciences markets. Operating facilities and sales, support and engineering facilities are located in North America, Europe and Asia.

We sell our products directly to original equipment manufacturers ("OEMs") and to their contract manufacturers and suppliers and to a lesser extent through distributors worldwide.

The following table shows the percentage of total revenue generated by each of our segments for the years ended December 31, 2014, 2013 and 2012:

	Revenue					
	Years Ended December 31,		2013		2012	
	2014	%	2013	%	2012	%
Mobile Consumer Electronics	60	%	64	%	60	%
Specialty Components	40	%	36	%	40	%

The following table shows total assets by segment at December 31, 2014 and 2013:  
(in millions)

	December 31,	
	2014	2013
Mobile Consumer Electronics	\$1,474.1	\$1,638.2
Specialty Components	525.8	538.7
Corporate / eliminations	(1.4	) (6.8
Total	\$1,998.5	\$2,170.1

## Market Trends

Our products serve a variety of end markets, notably, consumer mobile devices, medical technology, aerospace and defense and telecommunications and can generally be divided into two categories: MCE and SC, as described below.

**MCE**- Includes analog and digital microphones, MEMS microphones, surface mounted device microphones, receivers, speakers, integrated modules, multi-functional devices, ultrasonic sensors and integrated audio sub-systems.

**SC**- Includes transducers, oscillators, capacitors and filters.

The markets served by MCE continue to be driven by trends in smartphone and tablet innovation and demand. Today, mobile device OEMs are facing ever-rising challenges to differentiate their products in the global marketplace while managing growing cost pressures and time-to-market expectations. However, mobile consumers and mobile carriers alike are expecting better quality voice calls, audio and video conferencing, capturing and playback, media content consumption and gaming, as well as extended battery life. To enable smart mobile devices to handle ever more demanding audio use cases, OEMs are increasingly adopting more intelligent active audio components (audio chipset) and higher performance passive acoustic components. Trends impacting the smartphone market today include:

**Smartphone growth from feature phone substitution.** The smartphones segment within the handset device market has exhibited consistently strong unit growth over the past several years. There continues to be a positive mix shift from the proliferation of lower-end smartphone devices and the further cannibalization of feature phones (i.e., non-smartphones). The average smartphone continues to drive higher audio content including more microphones and

higher value speakers than its feature phone counterpart, compounding the growth of acoustic content as mobile phone sales rise.

Smartphone OEM market share shifts are likely to remain volatile for some time. Over the past several years, Nokia, Blackberry and Samsung have lost significant market share to other United States and Asian-based OEMs who have released smartphones that have been more readily accepted due to, among other factors, perceived feature sets

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and price points. We expect the OEM market to continue to be dynamic over time, characterized by rapid market share shifts driven by new product introductions, price points and feature sets.

New OEM product line rollouts. Smartphones continue to shift to Long Term Evolution (“LTE”), a standard for 4G wireless technology and the shift is expected to buoy unit growth in developed markets and drive the competitive landscape in high-end chipsets through 2015. Aggressive LTE deployments are happening in

- China, in addition to a build-out of deeper coverage profiles in the United States, Japan, Korea and Northern Europe. Deployments are also expected to accelerate in emerging markets. This will likely drive an increase in LTE smartphone units over the next several years, which should help maintain some level of high-end smartphone volume growth despite high market penetration.

Shortened smartphone upgrade plans at U.S. carriers. Several U.S. carriers have recently introduced new smartphone plans which offer consumers the option of paying for their phone in monthly installments with no upfront lump sum payment and the ability to upgrade again in 12 months. Plans such as these could drive greater-than-expected unit growth (turnover) at the high end, as they are most likely to appeal to high-income consumers seeking to upgrade their phone more frequently.

High-end consumer elasticity. Consumers are reluctant to downgrade from a high-end smartphone to a low-end smartphone in most circumstances. This is especially true as high-end smartphones will likely continue to offer significant performance advantages and new functionality compared to low-end smartphones.

Proliferation of premium acoustics. Consumers are seeking improved acoustics solutions, regardless of the country they live in or the type of device they are using. As a result, acoustic dollar content is generally expanding per device for two primary reasons. First, many of the solutions we are introducing are higher performance and command higher value. Secondly, a majority of OEMs are increasing the number of acoustic components per device. Over the past several years, we have seen an increase in the number of microphones used in high end smartphones. The benefits to the user are substantial, including reduced background noise, improved voice recognition, better hands-free communication and enhanced audio recording and playback capabilities. OEMs and their customers recognize the importance of these features in their next-generation products. We believe an additional opportunity exists for these trends to proliferate to mid-range phones and tablets, as well as emerging wearable devices. Knowles can capitalize on these market demands by leveraging our acoustics expertise and proprietary process technologies to deliver solutions that improve the performance of our OEM customers’ devices.

Specialty Components products are sold across diverse end markets and relative to the Acoustic Components end markets, portions of this business face much greater exposure to capital investment cycles and government spending, both direct and indirect, as some of these end markets are largely dependent on project upgrades, expansion and government contracts. These products can be divided into the following categories:

• Medical and life sciences products (i.e., transducers, hearing aids, capacitors). Product sales are largely driven by aging demographics, healthcare spending, the rise of a middle class in emerging markets and government subsidies.

• Aerospace and defense communications (i.e., capacitors, filters, oscillators). Aerospace and defense spending and automation (largest end market), telecom regional coverage and bandwidth expansion and growing industrial power supply requirements are a few of the end market trends driving the product sales in this sector.

• Telecom infrastructure (i.e., capacitors, filters, oscillators). Sales are typically levered to the expansion of large telecom companies, looking to increase wireless signal in new or existing territories, although these products are also sold to aerospace and defense companies (i.e., airplane radio frequencies).

## Geographic Trends

We strive to maintain our manufacturing facilities in close proximity to our direct customers. In the case of MCE, we operate eight facilities in Asia to serve the contract manufacturers who build OEM equipment on behalf of our end-customers. These contract manufacturers are largely based in China, Taiwan and India. Although end-user

demand for consumer electronics is global and marketing activities occur globally, the majority of our manufacturing is located in Asia, primarily in China, Malaysia and the Philippines.

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In the case of SC, we operate five facilities in Asia to serve the manufacturing sites of both hearing aid OEMs and the contract manufacturers who build OEM headsets on behalf of earphone makers. These OEM manufacturing sites are largely based in China, Singapore, Indonesia and Vietnam. Although marketing activities and end-user demand for hearing aid and specialty consumer components is global, manufacturing is primarily located in Asia for the purposes of being close to the point of assembly. We also operate six facilities in North America and three in Europe for the manufacturing of capacitors and oscillators that support our global telecom and military customers, as well as their suppliers and contract manufacturers.

As a majority of our manufacturing and sales occur outside the United States, we generate the majority of our profits and cash outside the United States. While no significant statutory limitation exists, a repatriation of profits from foreign markets to the United States is inherently inefficient.

### Competitive Landscape

Success in the electronic components industry is primarily driven by innovation and flexibility as customers compete to gain a share of the growing consumer device market. We compete across handset, tablet and other consumer platforms to deliver superior acoustic performance through customized products. Our continuous investment in research and development enables us to capture new design wins across consumer OEMs. Flexibility in balancing full and semi-automation is key to achieving a superior cost structure. Additionally, it is important for suppliers to have flexibility and quick time-to-market to meet clients' needs. Notably, according to industry estimates, the product cycle for handsets has shortened over recent years. Key competitors include:

MCE- AAC Technologies, Goertek, ST Micro and Invensense; and  
SC- Sonion, Rakon, Kyocera, and Epson Electronics.

In the MCE segment, our investments in research and development enable us to continually introduce new products with higher performance. Our customers are adopting these higher value microphones, speakers and receivers to improve the overall audio performance of their devices which in turn improves the end user experience. Typically our new products have higher average selling prices than the products they are replacing. Once introduced, the pricing for these products follows a normal downward trend as typically seen in the consumer electronics market. Some OEMs are moving to our higher value integrated module and intelligent audio solutions to enable additional performance advantages.

For products that were introduced more than 18 months ago, we strive to offset anticipated price erosion through bill of material cost reductions, yield improvements, equipment efficiency and movement to lower-cost manufacturing locations.

In the SC segment, the end markets tend to be more stable. Within acoustics we see limited competition but continuously invest to improve acoustic performance for our hearing health and high end headset customers. In precision devices we see a highly fragmented set of competitors across capacitor and oscillator products for a diverse set of end markets including telecom infrastructure, military, aerospace and medical.

### Customers, Sales and Distribution

We serve customers in the mobile consumer electronics, medical technology, defense/aerospace, telecommunication infrastructure and other industrial markets. Our customers include some of the largest operators in these markets. In addition, many of our OEM customers outsource their manufacturing to Electronic Manufacturing Services ("EMS") companies. Other customers include global mobile phone and hearing aid manufacturers and many of the largest

global EMS companies, particularly in China. For the year ended December 31, 2014, Apple, Inc. and Samsung Group accounted for approximately 20% and 12%, respectively, of our total revenue. For the year ended December 31, 2013, Apple, Inc. and Samsung Group accounted for approximately 25% and 15%, respectively, of our total revenue. For the year ended December 31, 2012, Apple, Inc. accounted for 18% of our total revenue. No other customer accounted for more than 10% of total revenues during these periods.

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The following table details our sales by geographic location for the years ended December 31, 2014, 2013 and 2012. These results do not necessarily indicate the geographies where our products are deployed or where end-customer demand is originated.

(in millions)	Years Ended December 31,		
	2014	2013	2012
Asia	\$879.0	\$950.4	\$855.5
Europe	120.4	120.8	110.6
Other Americas	12.4	14.5	15.2
Other	5.1	6.0	6.8
Subtotal non-United States	\$1,016.9	\$1,091.7	\$988.1
United States	124.4	123.1	129.9
Total	\$1,141.3	\$1,214.8	\$1,118.0

We own and conduct manufacturing operations through a network of facilities throughout the world. We also maintain quality assurance, manufacturing technology, supply chain and distribution departments. Our global distribution center is located in Penang, Malaysia. For our long-lived assets by geographic region, see Note 14. Segment Information of the notes to our Consolidated Financial Statements under Item 8, "Financial Statements and Supplementary Data."

## Raw Materials

We use a wide variety of raw materials, primarily metals and