

SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 28, 2003
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 0-31051

SMTC CORPORATION

(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

DELAWARE
(STATE OR OTHER JURISDICTION OF INCORPORATION
OR ORGANIZATION)

98-0197680
(I.R.S. EMPLOYER
IDENTIFICATION NO.)

635 HOOD ROAD
MARKHAM, ONTARIO, CANADA L3R 4N6
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES) (ZIP CODE)

(905) 479-1810
(REGISTRANT'S TELEPHONE NUMBER, INCLUDING AREA CODE)

Indicate by check mark whether SMTC Corporation: (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 is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes No .

As of November 7, 2003, SMTC Corporation had 24,095,968 shares of common stock, par value \$0.01 per share, and one share of special voting stock, par value \$0.01 per share, outstanding. As of November 7, 2003, SMTC Corporation's subsidiary, SMTC Manufacturing Corporation of Canada, had 4,593,811 exchangeable shares outstanding, each of which is exchangeable into one share of common stock of SMTC Corporation.

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**SMTC Corporation
Form 10-Q**

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SMTC CORPORATION

Consolidated Balance Sheets
(expressed in thousands of U.S. dollars)

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

	September 28, 2003	December 31, 2002
	(unaudited)	
Assets		
Current assets:		
Cash	\$ 621	\$ 370
Accounts receivable, net of an allowance for doubtful accounts of \$2,094 (December 31, 2002—\$2,097)	51,000	57,398
Inventories (note 3)	35,163	38,362
Prepaid expenses	1,438	2,611
Income taxes recoverable	—	841
	88,222	99,582
Capital assets	32,331	43,677
Other assets	6,129	13,378
Deferred income taxes (note 6)	—	34,325
	\$ 126,682	\$ 190,962
Liabilities and Shareholders' Equity (Deficit)		
Current liabilities:		
Accounts payable	\$ 47,008	\$ 56,165
Accrued liabilities	23,168	33,814
Income taxes payable	266	—
Current portion of long-term debt (note 4)	11,942	17,500
Current portion of capital lease obligations	266	257
	82,650	107,736
Long-term debt (note 4)	62,980	65,089
Capital lease obligations	15	176
Shareholders' equity (deficit):		
Capital stock	64,266	66,802
Warrants	1,523	1,255
Loans receivable	(5)	(5)
Additional paid-in-capital	165,896	163,360
Deficit	(250,643)	(213,451)
	(18,963)	17,961
Guarantees (note 11)		
	\$ 126,682	\$ 190,962

See accompanying notes to consolidated financial statements.

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Consolidated Statements of Operations

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

(Unaudited)

	Three months ended		Nine months ended	
	September 28, 2003	September 29, 2002 (restated – note 9)	September 28, 2003	September 29, 2002 (restated – note 9)
Revenue	\$ 76,973	\$ 143,520	\$ 229,220	\$ 416,040
Cost of sales, including restructuring and other charges (note 8)	68,828	142,532	208,393	404,192
Gross profit	8,145	988	20,827	11,848
Selling, general and administrative expenses	4,562	6,015	14,019	17,954
Amortization	997	639	2,941	1,695
Restructuring and other charges (recoveries) (note 8)	8	6,441	(113)	6,441
Operating income (loss)	2,578	(12,107)	3,980	(14,242)
Interest	1,072	1,928	3,911	6,630
Earnings (loss) before income taxes, discontinued operations and the cumulative effect of a change in accounting policy	1,506	(14,035)	69	(20,872)
Income tax expense (recovery) (note 6)	204	(36)	34,839	(1,368)
Earnings (loss) from continuing operations	1,302	(13,999)	(34,770)	(19,504)
Earnings (loss) from discontinued operations (note 9)	1,329	583	(2,422)	(8,394)
Cumulative effect of a change in accounting policy (note 10)	—	—	—	(55,560)
Net earnings (loss)	\$ 2,631	\$ (13,416)	\$ (37,192)	\$ (83,458)

See accompanying notes to consolidated financial statements.

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SMTC CORPORATION

Consolidated Statements of Operations (continued)

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

(Unaudited)

	Three months ended		Nine months ended	
	September 28, 2003	September 29, 2002 (restated – note 9)	September 28, 2003	September 29, 2002 (restated – note 9)
Earnings (loss) per share:				
Basic earnings (loss) per share from continuing operations	\$ 0.04	\$ (0.49)	\$ (1.21)	\$ (0.68)
Earnings (loss) from discontinued operations per share	0.05	0.02	(0.09)	(0.30)
Loss from the cumulative effect of a change in accounting policy per share	—	—	—	(1.93)
Basic earnings (loss) per share	\$ 0.09	\$ (0.47)	\$ (1.30)	\$ (2.91)
Diluted earnings (loss) per share	\$ 0.09	\$ (0.47)	\$ (1.30)	\$ (2.91)
Weighted average number of shares used in the calculations of earnings (loss) per share (note 5):				
Basic	28,689,779	28,689,779	28,689,779	28,689,779
Diluted	28,697,555	28,689,779	28,689,779	28,689,779

See accompanying notes to consolidated financial statements.

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SMTC CORPORATION

Consolidated Statement of Changes in Shareholders' Equity (Deficit)

(Expressed in thousands of U.S. dollars)

Nine months ended September 28, 2003

(Unaudited)

	<u>Capital stock</u>	<u>Warrants</u>	<u>Additional paid-in capital</u>	<u>Loans receivable</u>	<u>Deficit</u>	<u>Shareholders' equity (deficit)</u>
Balance, December 31, 2002	\$66,802	\$ 1,255	\$163,360	\$ (5)	\$(213,451)	\$ 17,961
Conversion of shares from exchangeable to common stock	(2,536)	—	2,536	—	—	—
Warrants issued	—	110	—	—	—	110
Warrants to be issued	—	158	—	—	—	158
Net loss for the period	—	—	—	—	(37,192)	(37,192)
Balance, September 28, 2003	<u>\$64,266</u>	<u>\$ 1,523</u>	<u>\$165,896</u>	<u>\$ (5)</u>	<u>\$(250,643)</u>	<u>\$ (18,963)</u>

See accompanying notes to consolidated financial statements.

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(Expressed in thousands of U.S. dollars)

(Unaudited)

	Three months ended		Nine months ended	
	September 28, 2003	September 29, 2002	September 28, 2003	September 29, 2002
Cash provided by (used in):				
Operations:				
Net earnings (loss)	\$ 2,631	(13,416)	\$ (37,192)	\$ (83,458)
Items not involving cash:				
Amortization	997	639	2,941	1,695
Depreciation	1,735	3,047	6,465	9,082
Deferred income tax expense (benefit)	—	(12)	34,325	(1,224)
Gain on disposition of assets	—	1	(25)	(24)
Impairment of assets (note 8)	37	—	37	1,129
Loss on disposition of discontinued operation (note 9)	235	—	3,461	—
Gain on disposal of assets previously written down (note 8)	(69)	—	(277)	—
Discount on prepayment of shareholder loans (note 8)	—	—	389	—
Write-down of goodwill (note 10)	—	—	—	55,560
Change in non-cash operating working capital:				
Accounts receivable	(8,354)	10,705	4,496	11,095
Inventories	(5,468)	31,842	2,157	31,497
Prepaid expenses	166	2,056	1,117	1,467
Income taxes recoverable	517	(175)	1,107	301
Accounts payable	(414)	(4,466)	(7,757)	1,263
Accrued liabilities	(2,525)	(6,524)	(10,255)	(2,934)
	(10,512)	23,697	989	25,449
Financing:				
Increase in long-term debt	15,820	—	7,891	—
Repayment of long-term debt	(8,058)	(23,873)	(15,558)	(32,634)
Principal payments on capital lease obligations	(57)	(31)	(152)	(136)
Repayment of shareholder loans	—	8	3,795	8
Debt issuance costs	—	—	—	(2,031)
	7,705	(23,896)	(4,024)	(34,793)
Investments:				
Purchase of capital assets	(49)	(200)	(137)	(2,510)
Proceeds from sale of capital assets	102	58	335	159
Proceeds from sale of discontinued operation (note 9)	3,058	—	3,058	—
Other	—	250	30	250
	3,111	108	3,286	(2,101)
Increase (decrease) in cash	304	(91)	251	(11,445)
Cash, beginning of period	317	749	370	12,103
Cash, end of period	\$ 621	\$ 658	\$ 621	\$ 658

See accompanying notes to consolidated financial statements.

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SMTC CORPORATION

Consolidated Statements of Cash Flows (continued)

(Expressed in thousands of U.S. dollars)

(Unaudited)

	Three months ended		Nine months ended	
	September 28, 2003	September 29, 2002	September 28, 2003	September 29, 2002
Supplemental disclosures:				
Cash paid during the period:				
Income taxes	\$ —	\$ 344	\$ 144	\$ 1,644
Interest	1,278	—	2,662	4,365
Non-cash financing activities:				
Issuance of warrants	\$ 268	\$ —	\$ 268	\$ 659

See accompanying notes to consolidated financial statements.

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SMTC CORPORATION

Notes to Consolidated Financial Statements

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

Three and nine months ended September 28, 2003 and September 29, 2002

(Unaudited)

1. Basis of presentation:

The Company's accounting principles are in accordance with accounting principles generally accepted in the United States.

The accompanying unaudited consolidated balance sheet as at September 28, 2003, unaudited consolidated statements of operations for the three and nine month periods ended September 28, 2003 and September 29, 2002, unaudited consolidated statement of changes in shareholders' equity (deficit) for the nine month period ended September 28, 2003, and unaudited consolidated statements of cash flows for the three and nine month periods ended September 28, 2003 and September 29, 2002 have been prepared on substantially the same basis as the annual consolidated financial statements, except as described below. Management believes the consolidated financial statements reflect all adjustments, consisting only of normal recurring accruals, which are, in the opinion of management, necessary for a fair presentation of the Company's financial position, operating results and cash flows for the periods presented. The results of operations for the three and nine month periods ended September 28, 2003 are not necessarily indicative of results to be expected for the entire year. These unaudited interim consolidated financial statements should be read in conjunction with the annual consolidated financial statements and notes thereto for the year ended December 31, 2002.

The unaudited interim consolidated financial statements are based upon accounting principles consistent with those described in the December 31, 2002 audited consolidated financial statements except as follows:

In August 2001, the Financial Accounting Standards Board ("FASB") issued Statement No. 143, Accounting for Asset Retirement Obligations, which requires that the fair value of an asset retirement obligation be recorded as a liability, at fair value, in the period in which the Company incurs the obligation. The Statement is effective for fiscal 2003 and there was no material effect as a result of the adoption of this Statement on January 1, 2003.

In July 2002, the FASB issued Statement No. 146, Accounting for Costs Associated with Exit or Disposal Activities ("Statement 146"), which nullifies Emerging Issues Task Force ("EITF") Issue 94-3, Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity ("EITF 94-3"). Statement 146 provides for the recognition of a liability for an exit or disposal activity only when a liability is incurred and can be measured at fair value. Under EITF 94-3, a commitment to an exit or disposal plan was sufficient to record the majority of the costs. Statement 146 is effective for exit or disposal activities initiated after December 31, 2002. The Company adopted this Statement on January 1, 2003 and accordingly, the restructuring charges recorded in the three and nine months ended September 28, 2003 were made in accordance with the new standard.

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Notes to Consolidated Financial Statements (continued)

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

Three and nine months ended September 28, 2003 and September 29, 2002

(Unaudited)

1. Basis of presentation (continued):

In November 2002, the FASB issued Interpretation (“FIN”) No. 45, Guarantor’s Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees and Indebtedness of Others, which requires certain disclosures of obligations under guarantees. The disclosure requirements of FIN 45 were effective for the Company’s year ended December 31, 2002. Effective for 2003, FIN 45 also requires the recognition of a liability by a guarantor at the inception of certain guarantees entered into or modified after December 31, 2002, based on the fair value of the guarantee. The Company adopted the disclosure requirements in its 2002 consolidated financial statements. The Company has not entered into or modified any guarantees after December 31, 2002. See note 11 for disclosure related to guarantees.

In January 2003, the FASB issued FIN No. 46, Consolidation of Variable Interest Entities, which requires variable interest entities, previously referred to as special-purpose entities or off-balance sheet structures, to be consolidated by a company if that company is subject to a majority of the risk of loss from the entity’s activities or is entitled to receive a majority of the entity’s returns or both. The consolidation provisions of FIN No. 46 apply immediately to variable interest entities created after January 31, 2003 and to existing entities in the first fiscal year or interim period ending after December 15, 2003. Certain disclosure provisions apply in financial statements issued after January 31, 2003. The consolidation requirements of FIN No. 46 are not expected to have a material effect on the Company’s consolidated financial statements.

In April 2003, the FASB issued Statement No. 149, Amendments of Statement 133 on Derivative Instruments and Hedging Activities (“Statement 149”), which amends and clarifies financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities under Statement 133. This statement is effective for contracts entered into or modified after June 30, 2003, with certain exceptions, and for hedging relationships designated after June 30, 2003. There was no material effect as a result of the adoption of this statement on July 1, 2003.

In May 2003, the FASB issued Statement No. 150, Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity (“Statement 150”), which establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. Financial instruments that are within the scope of the statement, which previously were often classified as equity, must now be classified as liabilities. This statement is effective for financial instruments entered into or modified after May 31, 2003, and otherwise shall be effective at the beginning of the first interim period after June 15, 2003. There was no material effect as a result of the adoption of this statement in the third quarter of 2003.

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Notes to Consolidated Financial Statements (continued)

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

Three and nine months ended September 28, 2003 and September 29, 2002

(Unaudited)

2. Stock-based compensation:

The Company accounts for stock options issued to employees using the intrinsic value method of Accounting Principles Board Opinion No. 25. Compensation expense is recorded on the date stock options are granted only if the current fair value of the underlying stock exceeds the exercise price. The Company has provided the pro forma disclosures required by FASB Statement No. 123, Accounting for Stock-Based Compensation ("Statement 123") as amended by Statement 148.

The table below sets out the pro forma amounts of net earnings (loss) and net earnings (loss) per share that would have resulted if the Company had accounted for its employee stock plans under the fair value recognition provisions of Statement 123.

	Three months ended		Nine months ended	
	September 28, 2003	September 29, 2002	September 28, 2003	September 29, 2002
Net earnings (loss), as reported	\$ 2,631	\$ (13,416)	\$ (37,192)	\$ (83,458)
Stock-based compensation expense	(274)	(286)	(932)	(824)
Pro forma earnings (loss)	2,357	(13,702)	(38,124)	(84,282)
Basic earnings (loss) per share, as reported	\$ 0.09	\$ (0.47)	\$ (1.30)	\$ (2.91)
Stock-based compensation expense	(0.01)	(0.01)	(0.03)	(0.02)
Pro forma basic earnings (loss) per share	0.08	(0.48)	(1.33)	(2.93)
Diluted earnings (loss) per share, as reported	\$ 0.09	\$ (0.47)	\$ (1.30)	\$ (2.91)
Stock-based compensation expense	(0.01)	(0.01)	(0.03)	(0.02)
Pro forma diluted earnings (loss) per share	0.08	(0.48)	(1.33)	(2.93)

No compensation expense related to stock options has been recorded in the statement of operations for the three and nine months ended September 28, 2003 and September 29, 2002.

The weighted average estimated fair value at the date of the grant for the options granted during the nine months ended September 28, 2003 was \$0.59 per share (2002—\$1.00).

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Notes to Consolidated Financial Statements (continued)

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

Three and nine months ended September 28, 2003 and September 29, 2002

(Unaudited)

2. Stock-based compensation (continued):

The estimated fair value of options is calculated at the date of grant, is amortized over the vesting period, on a straight-line basis, and was determined using the Black-Scholes option pricing model using the following assumptions:

	Nine months ended	
	September 28, 2003	September 29, 2002
Risk-free interest rate	4.0%	5.0%
Dividend yield	—	—
Expected life	4 years	4 years
Volatility	120.0%	120.0%

During the second quarter of 2003, the Company granted 40,000 options to purchase common stock at an exercise price of \$0.75 per share, the fair market value on the date of grant. No options to purchase common stock were granted during the third quarter of 2003.

3. Inventories:

	September 29, 2003	December 31, 2002
Raw materials	\$ 18,681	\$ 15,665
Work in process	8,133	9,712
Finished goods	7,705	12,093
Other	644	892
	<u>\$ 35,163</u>	<u>\$ 38,362</u>

4. Long-term debt:

During November, 2003, the Company and its lending group executed an amendment to the credit agreement with an effective date of November 17, 2003 (the "Effective Date"), providing for a waiver of certain events of default, if any, arising prior to the Effective Date. The Company and its lending group also amended the credit facility to provide for term loans of \$11,942 and revolving credit loans, swing-line loans and letters of credit of \$80,000 with an extension of the maturity date to October 1, 2004 and amendments of certain financial and other covenants based on the Company's current business plan. During the amendment period, the facility bears interest at the U.S. base rate plus 0.25% to 2.5%.

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SMTC CORPORATION

Notes to Consolidated Financial Statements (continued)

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

Three and nine months ended September 28, 2003 and September 29, 2002

(Unaudited)

4. Long-term debt (continued):

The Company was in compliance with the financial covenants at September 28, 2003. Continued compliance with the amended financial covenants through to October 1, 2004 is dependent on the Company achieving the forecasts inherent in its current business plan. The Company believes the forecasts are based on reasonable assumptions; however, the forecasts are dependent on a number of factors, some of which are outside the control of the Company. These include, but are not limited to, general economic conditions and specifically the strength of the electronics industry and the related demand for the products and services by the Company's customers. In the event of non-compliance, the Company's lenders have the right to demand repayment of all outstanding amounts under the amended credit facility. If the Company was unable to repay such amounts, the lenders could proceed against any collateral granted to them to secure the indebtedness. Substantially all of the Company's assets have been pledged to the lenders as collateral for the Company's obligations under the senior credit facility.

The Company's revolving credit facility matures on October 1, 2004 and accordingly as at September 28, 2003, this amount has been classified as a long-term liability. The Company has initiatives underway to refinance its bank indebtedness including discussions with current and potential lenders and investors. A transaction resulting from these discussions is likely to involve significant dilution to existing shareholders. To date no agreements have been reached and there can be no assurances that any agreement will be reached. Should the Company not be able to refinance the debt prior to October 1, 2004, the Company expects that it will be unable to repay the full amount of the debt upon maturity. In that event, or the event of any earlier default under the credit agreement, the Company would attempt to negotiate with its current lenders to modify the terms of the credit agreement. There can be no assurances that the Company will be able to negotiate or reach an agreement with its current lenders to modify the terms of the credit agreement.

Warrants:

In connection with the December 31, 2002 amendment to the credit agreement, the Company agreed to issue to the lenders warrants to purchase common stock of the Company at an exercise price equal to the fair market value (defined as average of the last reported sales price of the common stock of the company for twenty consecutive trading days commencing 22 trading days before the date in question) at the date of the grant for (a) 4.0% of the total outstanding shares on December 31, 2002, (b) 1.0% of the total outstanding shares on December 31, 2002, (c) 0.75% of the total outstanding shares on the date that is 45 days after the end of the Company's first fiscal quarter of 2003, (d) 0.75% of the total outstanding shares on the date that is 45 days after the end of the Company's second fiscal quarter of 2003 (the "Series D" warrants), (e) 0.75% of the total outstanding shares on the date that is 45 days after the end of the Company's third fiscal quarter of 2003 (the "Series E" warrants), (f) 0.75% of the total outstanding shares on the date that is 90 days after the end of the Company's fourth fiscal quarter of 2003, (g) 1.0% of the total outstanding shares on the date that is 45 days after the

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SMTC CORPORATION

Notes to Consolidated Financial Statements (continued)

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

Three and nine months ended September 28, 2003 and September 29, 2002

(Unaudited)

4. Long-term debt (continued):

end of the Company's first fiscal quarter of 2004 and (h) 1.0% of the total outstanding shares on the date that is 45 days after the end of the Company's second fiscal quarter of 2004; provided, however that if the Company meets certain EBITDA targets on the dates identified in (c) through (h) above, it will not issue warrants corresponding to such date. The Company met its EBITDA target as at March 30, 2003. The Company did not meet its EBITDA target at June 29, 2003 and 228,210 warrants were issued in the third quarter of 2003 with an effective date of August 13, 2003 at an exercise price of \$0.61 per share. Also, the Company did not meet its EBITDA target at September 28, 2003 and will issue 229,934 warrants in the fourth quarter of 2003 with an effective date of November 12, 2003 at an exercise price of \$1.04 per share.

The estimated fair value of the Series D and Series E warrants were measured using a Black-Scholes model at the respective issuance dates using the following assumptions:

Risk-free interest rate	4.0%
Dividend yield	—
Expected life	5 years
Volatility	125.0%

The estimated fair values of the Series D warrants of \$110 and the Series E warrants to be issued of \$158 have been classified in shareholders' equity.

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SMTC CORPORATION

Notes to Consolidated Financial Statements (continued)

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

Three and nine months ended September 28, 2003 and September 29, 2002

(Unaudited)

5. Earnings (loss) per share:

The following table sets forth the calculation of basic and diluted loss per share:

	Three months ended		Nine months ended	
	September 28, 2003	September 29, 2002	September 28, 2003	September 29, 2002
Numerator:				
Net earnings (loss) from continuing operations	\$ 1,302	\$ (13,999)	\$ (34,770)	\$ (19,504)
Net earnings (loss)	2,631	(13,416)	(37,192)	(83,458)
Denominator:				
Weighted average shares—basic	28,689,779	28,689,779	28,689,779	28,689,779
Effect of dilutive securities:				
Employee stock options	—	—	—	—
Warrants	7,776	—	—	—
Weighted-average shares—diluted	28,697,555	28,689,779	28,689,779	28,689,779
Earnings (loss) per share:				
Basic and diluted, from continuing operations	\$ 0.04	\$ (0.49)	\$ (1.21)	\$ (0.68)
Basic and diluted	0.09	(0.47)	(1.30)	(2.91)

Options and warrants to purchase common stock were outstanding during the nine month period ended September 28, 2003 and the three and nine month periods ended September 29, 2002 but were not included in the computation of diluted loss per share because their effect would be anti-dilutive on the earnings (loss) per share for the period.

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Notes to Consolidated Financial Statements (continued)

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

Three and nine months ended September 28, 2003 and September 29, 2002

(Unaudited)

6. Income taxes:

In assessing the realization of deferred tax assets, management considers whether it is more likely than not that some portion or all of its deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income. Management considers the scheduled reversal of deferred tax liabilities, change of control limitations, projected future taxable income and tax planning strategies in making this assessment. FAS 109 states that forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence such as cumulative losses in recent years in the jurisdictions to which the deferred tax assets relate. As a result of the quarterly review undertaken at the end of the second quarter, the Company concluded that given the weakness and uncertainty in the current economic environment, it was appropriate to establish a full valuation allowance for the deferred tax assets arising from its operations in the jurisdictions to which the deferred tax assets relate. As a result, the total valuation allowance for deferred tax assets in all jurisdictions worldwide increased from approximately \$35,000 at December 31, 2002 to approximately \$71,000 at June 29, 2003, resulting in income tax expense during the quarter ended June 29, 2003, of approximately \$34,200. In addition, the valuation allowance at September 28, 2003 remained at approximately \$71,000. The Company expects to provide a full valuation allowance on future tax benefits until it can demonstrate a sustained level of profitability that establishes its ability to utilize the assets in the jurisdictions to which the assets relate.

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Notes to Consolidated Financial Statements (continued)

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

Three and nine months ended September 28, 2003 and September 29, 2002

(Unaudited)

7. Segmented information:

The Company derives its revenue from one dominant industry segment, the electronics manufacturing services industry. The Company is operated and managed geographically and has four facilities in the United States, Canada and Mexico. The Company monitors the performance of its geographic operating segments based on EBITA (earnings before interest, taxes and amortization) before restructuring charges, discontinued operations and the effect of changes in accounting policies. Discontinued operations relate to the Cork, Ireland facility, which was previously included in the results of the European segment and the sale of the Appleton manufacturing operations, previously included in the results of the United States segment (note 9). Intersegment adjustments reflect intersegment sales that are generally recorded at prices that approximate arm's-length transactions. Information about the operating segments is as follows:

	Three months ended September 28, 2003			Nine months ended September 28, 2003		
	Total revenue	Intersegment revenue	Net external revenue	Total revenue	Intersegment revenue	Net external revenue
United States	\$ 22,680	\$ (7,775)	\$14,905	\$124,395	\$ (12,289)	\$112,106
Canada	65,553	(3,508)	62,045	130,181	(14,643)	115,538
Europe	—	—	—	2,542	(1,079)	1,463
Mexico	51,767	(51,744)	23	115,015	(114,902)	113
	<u>\$140,000</u>	<u>\$ (63,027)</u>	<u>\$76,973</u>	<u>\$372,133</u>	<u>\$ (142,913)</u>	<u>\$229,220</u>

EBITA (before discontinued operations, restructuring charges and the cumulative effect of a change in accounting policy):

United States	\$ (1,023)	\$ (1,147)
Canada	(228)	(1,198)
Europe	37	126
Mexico	4,233	8,074
	<u>3,019</u>	<u>5,855</u>
Interest	1,072	3,911
Amortization	997	2,941
Restructuring charges (recoveries) (note 8)	(556)	(1,066)
Earnings before income taxes, discontinued operations and the cumulative effect of a change in accounting policy	<u>\$ 1,506</u>	<u>\$ 69</u>
Capital expenditures:		
United States	\$ —	\$ 71
Canada	43	43
Mexico	6	23
	<u>\$ 49</u>	<u>\$ 137</u>

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SMTC CORPORATION

Notes to Consolidated Financial Statements (continued)

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

Three and nine months ended September 28, 2003 and September 29, 2002

(Unaudited)

7. Segmented information (continued):

(restated – note 9)

	Three months ended September 29, 2002			Nine months ended September 29, 2002		
	Total revenue	Intersegment revenue	Net external revenue	Total revenue	Intersegment revenue	Net external revenue
United States	\$117,405	\$ (2,044)	\$115,361	\$354,540	\$ (14,571)	\$339,969
Canada	30,184	(3,289)	26,895	78,584	(9,236)	69,348
Europe	1,090	—	1,090	4,050	(501)	3,549
Mexico	53,582	(53,408)	174	148,056	(144,882)	3,174
	<u>\$202,261</u>	<u>\$ (58,741)</u>	<u>\$143,520</u>	<u>\$585,230</u>	<u>\$ (169,190)</u>	<u>\$416,040</u>

EBITA (before discontinued operations, restructuring charges and the cumulative effect of a change in accounting policy):

United States	\$ 1,875	\$ (2,061)
Canada	(579)	(59)
Europe	925	519
Mexico	(962)	1,781
	<u>1,259</u>	<u>180</u>
Interest	1,928	6,630
Amortization	639	1,695
Restructuring charges	12,727	12,727
Loss before income taxes, discontinued operations and the cumulative effect of a change in accounting policy	<u>\$ (14,035)</u>	<u>\$ (20,872)</u>
Capital expenditures:		
United States	\$ 9	\$ 1,419
Canada	135	678
Europe	—	26
Mexico	56	387
	<u>\$ 200</u>	<u>\$ 2,510</u>

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SMTC CORPORATION

Notes to Consolidated Financial Statements (continued)

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

Three and nine months ended September 28, 2003 and September 29, 2002

(Unaudited)

7. Segmented information (continued):

The following enterprise-wide information is provided. Geographic revenue information reflects the destination of the product shipped. Long-lived assets information is based on the principal location of the asset.

	Three months ended		Nine months ended	
	September 28, 2003	September 29, 2002	September 28, 2003	September 29, 2002
		(restated – note 9)		(restated – note 9)
Geographic revenue:				
United States	\$ 64,910	\$ 105,712	\$ 187,015	\$ 312,351
Canada	11,967	8,421	28,001	28,922
Europe	—	14,994	6,001	40,253
Asia	—	10,087	3,613	24,197
Mexico	96	4,306	4,590	10,317
	<u>\$ 76,973</u>	<u>\$ 143,520</u>	<u>\$ 229,220</u>	<u>\$ 416,040</u>
			September 28, 2003	December 31, 2002
Long-lived assets:				
United States			\$ 12,901	\$ 21,080
Canada			3,007	4,618
Mexico			16,423	17,979
			<u>\$ 32,331</u>	<u>\$ 43,677</u>

The Company manufactures a limited number of products for each customer. If the Company loses any of its largest customers or any product line manufactured for one of its largest customers, it could experience a significant reduction in revenue. Also, the insolvency of one or more of its largest customers or the inability of one or more of its largest customers to pay for its orders could decrease revenue. As many costs and operating expenses are relatively fixed, a reduction in net revenue can decrease profit margins and adversely affect business, financial condition and results of operations.

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SMTC CORPORATION

Notes to Consolidated Financial Statements (continued)

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

Three and nine months ended September 28, 2003 and September 29, 2002

(Unaudited)

8. Restructuring and other charges:

The following table relates to the components of the restructuring and other charges for the three and nine months ended September 28, 2003 and September 29, 2002:

	Three months ended		Nine months ended	
	September 28, 2003	September 29, 2002	September 28, 2003	September 29, 2002
Inventory write-downs included in cost of sales	\$ —	\$ 6,286	\$ —	\$ 6,286
Lease and other contract obligations	2,382	5,790	2,504	5,790
Adjustments of previously recorded lease and other contract obligations	(3,462)	(393)	(4,123)	(393)
Severance	1,121	1,044	1,677	1,044
Other facility exit costs	52	—	52	—
Adjustments to other facility exit costs	(617)	—	(920)	—
Asset impairment	37	—	37	—
Proceeds on assets previously written down	(69)	—	(293)	—
	<u>(556)</u>	<u>6,441</u>	<u>(1,066)</u>	<u>6,441</u>
	<u>(556)</u>	<u>12,727</u>	<u>(1,066)</u>	<u>12,727</u>
Other charges included in restructuring and other charges	564	—	953	—
Other charges included in cost of sales	—	900	—	900
	<u>\$ 8</u>	<u>\$ 13,627</u>	<u>\$ (113)</u>	<u>\$ 13,627</u>

2001 Restructuring Plan:

During fiscal year 2001, in response to excess capacity caused by slowing technology end markets, the Company commenced a restructuring program aimed at reducing its cost structure. During the third quarter of 2003, the Company recorded lease and other contract obligations of \$2,178 related to additional costs associated with the facility lease in Monterrey, Mexico. Also, during the third quarter of 2003 the Company recorded an adjustment to its initial 2001 restructuring plan of \$219 due to the Company settling certain obligations for less than the original estimated amounts.

The following table details the related amounts included in accrued liabilities as at September 28, 2003 relating to the 2001 plan:

	Accrual at June 29, 2003	2003 charges	2003 adjustments	Cash payments	Accrual at September 28, 2003
Lease and other contract obligations	\$ 1,071	\$2,178	\$ —	\$ (183)	\$ 3,066
Other facility exit costs	283	—	(219)	(61)	3
	<u>\$ 1,354</u>	<u>\$2,178</u>	<u>\$ (219)</u>	<u>\$ (244)</u>	<u>\$ 3,069</u>

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Notes to Consolidated Financial Statements (continued)

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

Three and nine months ended September 28, 2003 and September 29, 2002

(Unaudited)

8. Restructuring and other charges (continued):

2002 Restructuring Plan:

In response to the continuing industry economic downturn, the Company took further steps to realign its cost structure and plant capacity and in the third and fourth quarters of 2002 recorded restructuring charges of \$37,444 related to the cost of exiting equipment and facility leases, severance costs, asset impairment charges, inventory exposures and other facility exit costs and other charges of \$2,135 primarily related to the costs associated with the disengagement of a customer and the continued downturn.

The Company recorded further charges related to the 2002 plan during the three and nine months ended September 28, 2003 of \$1,414 and \$2,092, respectively. Lease and other contract obligations of \$204 recorded in the third quarter of 2003 relate largely to additional costs associated with idling equipment leases at the Donegal facility. Severance costs of \$1,121 recorded during the third quarter of 2003 include \$891 related to the closure of the Charlotte facility and resizing of other facilities. The severance costs related to 96 plant and operational employees, primarily at the Charlotte facility. Other facility exit costs of \$52 recorded in the third quarter of 2003 relate largely to costs associated with closing the Charlotte facility. The Company recorded adjustments to its initial 2002 restructuring plan for the three and nine months ended September 28, 2003 of \$3,929 and \$5,117, respectively. Adjustments to previously recorded lease and other contract obligations of \$3,462 and other facility exit costs of \$398 recorded during the third quarter of 2003 relate to the Company revising its original estimates associated with the costs of closing the Austin and Charlotte facilities, based on the settlement of certain liabilities for less than previously estimated and the effects of ongoing negotiations. The Company also recorded an asset impairment charge of \$37 related to the write-down of assets at the Charlotte facility and a gain of \$69 related to the disposal of assets previously written down at the Donegal facility.

The following table details the related amounts included in accrued liabilities as at September 28, 2003 related to the 2002 plan:

	Accrual at June 29, 2003	2003 charges	2003 adjustments	Cash payments	Accrual at September 28, 2003
Lease and other contract obligations	\$ 12,960	\$ 204	\$ (3,462)	\$(1,580)	\$ 8,122
Severance	96	1,121	—	(1,217)	—
Other facility exit costs	1,021	52	(398)	(290)	385
	<u>\$ 14,077</u>	<u>\$ 1,377</u>	<u>\$ (3,860)</u>	<u>\$(3,087)</u>	<u>\$ 8,507</u>

Other charges recorded during the third quarter of 2003 of \$564 relate to professional fees associated with the Company's refinancing negotiations with current and potential lenders and investors.

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Notes to Consolidated Financial Statements (continued)

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

Three and nine months ended September 28, 2003 and September 29, 2002

(Unaudited)

9. Discontinued Operations:

(a) Appleton:

During the third quarter of 2003, the Company sold the manufacturing operations of the Appleton facility for cash proceeds of \$3,058. The Appleton facility has historically been included in the results of the United States segment (note 7). The Company recorded a loss on disposal of discontinued operation of \$235 which has been included in the loss from discontinued operations. Details of the net assets disposed of are as follows:

Proceeds on disposal of discontinued operation	\$ 3,058
Accounts receivable	1,902
Inventory	1,042
Prepaid expenses	56
Capital assets	1,722
Accounts payable	(1,400)
Accrued liabilities	(476)
	<hr/>
Net assets disposed of	2,846
Costs of disposal	447
	<hr/>
Loss on disposal of discontinued operation	\$ 235
	<hr/>

The following information included in discontinued operations relates to the sale of the Appleton manufacturing operations:

	Three months ended		Nine months ended	
	September 28, 2003	September 29, 2002	September 28, 2003	September 29, 2002
Revenue	\$ 2,485	\$ 9,423	\$ 10,750	\$ 37,401
Earnings (loss) from discontinued operations	\$ (235)	\$ 583	\$ (3,986)	\$ 1,803

Included in the earnings (loss) from discontinued operations for the nine months ended September 28, 2003 is the loss on disposition of discontinued operation of \$235, a restructuring charge of \$3,226 recorded during the second quarter of 2003, reflecting the write-down of the Appleton assets to the estimated realizable value and loss from operations of \$525.

The Company recorded an accrual for closing costs related to the disposition of the Appleton manufacturing operations of \$447. The remaining accrual at September 28, 2003 relating to the disposition is \$264.

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SMTC CORPORATION

Notes to Consolidated Financial Statements (continued)

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

Three and nine months ended September 28, 2003 and September 29, 2002

(Unaudited)

9. Discontinued Operations (continued):

(b) Cork:

In February 2002, the main customer of the Cork, Ireland facility was placed into administration as part of a financial restructuring. As a result, on March 19, 2002, the Company announced that it was closing the Cork, Ireland facility and that it was taking steps to place the subsidiary that operated that facility in voluntary administration. During the first quarter of 2002, the Company recorded a charge of \$9,717 related to the closure of the facility. During the third quarter of 2003 the Company received a distribution from the proceeds of the liquidation of \$2,304 and recorded additional charges of \$740 related to the wind-down of the facility and related operations.

The following information included in discontinued operations relates to the closure of the Cork facility:

	Three months ended		Nine months ended	
	September 28, 2003	September 29, 2002	September 28, 2003	September 29, 2002
Revenue	\$ —	\$ —	\$ —	\$ 5,035
Earnings (loss) from discontinued operations	\$ 1,564	\$ —	\$ 1,564	\$ (10,197)

In 2002, the loss from discontinued operations includes the costs of closing the facility of \$9,717. Included in this amount are the write-off of the net assets of \$6,717 (comprised of capital assets of \$1,129 and net working capital of \$5,588) and other costs associated with exiting the facility of \$3,000. Included in the other costs is severance of \$1,350 related to the termination of all employees. In 2003, the earnings from discontinued operations include the distribution from the proceeds of the liquidation of \$2,304, less additional charges of \$740 related to the wind-down of the facility and related operations.

The following table details the amounts included in accrued liabilities as at September 28, 2003 related to the closure of the Cork facility:

	Accrual at June 29, 2003	2003 charge	Cash payments	Accrual at September 28, 2003
Severance	\$ 188	\$ —	\$ (188)	\$ —
Other	—	740	(8)	732
	\$ 188	\$ 740	\$ (196)	\$ 732

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SMTC CORPORATION

Notes to Consolidated Financial Statements (continued)

(Expressed in thousands of U.S. dollars, except share quantities and per share amounts)

Three and nine months ended September 28, 2003 and September 29, 2002

(Unaudited)

10. Goodwill and Intangible Assets:

In July 2001, the FASB issued Statement No. 141, Business Combinations (“Statement 141”), and Statement No. 142, Goodwill and Other Intangible Assets (“Statement 142”). Statement 141 requires that the purchase method of accounting be used for all business combinations. Statement 141 also specifies criteria intangible assets acquired in a purchase method business combination must meet to be recognized and reported apart from goodwill. Statement 142 requires that goodwill and intangible assets with indefinite useful lives no longer be amortized, but instead tested for impairment at least annually in accordance with the provisions of Statement 142. Statement 142 also requires that intangible assets with definite useful lives be amortized over their respective estimated useful lives to their estimated residual values, and reviewed for impairment in accordance with Statement 144. Upon adoption of Statements 141 and 142 in their entirety on January 1, 2002, the Company determined that there were no intangible assets relating to previous acquisitions that need to be reclassified and accounted for apart from goodwill under the provisions of those Statements.

In connection with the transitional goodwill impairment evaluation, Statement 142 required the Company to perform an assessment of whether there was an indication that goodwill was impaired as of January 1, 2002. To accomplish this, the Company was required to identify its reporting units and determine the carrying value of each reporting unit by assigning the assets and liabilities, including the existing goodwill to those reporting units as of January 1, 2002. The Company identified its reporting units to be consistent with its business units, as defined in note 7, with the exception of the Boston, Massachusetts facility. This facility is not economically similar to the other U.S. facilities and as a result, is a separate reporting unit. In connection with the implementation of the new accounting standards, the Company completed the transitional goodwill impairment test, resulting in a goodwill impairment charge of \$55,560, which comprises the goodwill in the Canadian, U.S. and Boston reporting units of \$15,482, \$26,698 and \$13,380, respectively. The fair value of each reporting unit was determined using a discounted cash flow method. The transitional impairment loss was recognized as the cumulative effect of a change in accounting principle in the Company’s statements of operations as at January 1, 2002.

11. Guarantees:

Contingent liabilities in the form of letters of credit and letters of guarantee are provided to certain third parties, which cover payments for certain purchases. The total amount of future payments to be made under these guarantees is \$858.

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

SELECTED CONSOLIDATED FINANCIAL DATA

The consolidated financial statements and our selected consolidated financial data have been prepared in accordance with United States GAAP.

Consolidated Statement of Operations Data:
(in millions, except per share amounts)

(Unaudited)

	Three months ended		Nine months ended	
	September 28, 2003	September 29, 2002	September 28, 2003	September 29, 2002
		(Restated)		(Restated)
Revenue	\$ 77.0	\$ 143.5	\$ 229.2	\$ 416.1
Cost of sales, including restructuring and other charges (a)	68.8	142.6	208.4	404.2
Gross profit	8.2	0.9	20.8	11.9
Selling, general and administrative expenses	4.6	6.0	14.0	18.0
Amortization	1.0	0.6	2.9	1.7
Restructuring and other charges (recoveries) (a)	—	6.4	(0.1)	6.4
Operating income (loss)	2.6	(12.1)	4.0	(14.2)
Interest	1.1	1.9	3.9	6.6
Earnings (loss) before income taxes, discontinued operations and the cumulative effect of a change in accounting policy	1.5	(14.0)	0.1	(20.8)
Income tax expense (recovery) (b)	0.2	0.0	34.9	(1.3)
Earnings (loss) from continuing operations	1.3	(14.0)	(34.8)	(19.5)
Earnings (loss) from discontinued operations (c)	1.3	0.6	(2.4)	(8.4)
Cumulative effect of a change in accounting policy (d)	—	—	—	(55.6)
Net earnings (loss)	\$ 2.6	\$ (13.4)	\$ (37.2)	\$ (83.5)
Net earnings (loss) per share:				
Basic earnings (loss) per share from continuing operations	\$ 0.04	\$ (0.49)	\$ (1.21)	\$ (0.68)
Earnings (loss) from discontinued operations per share	0.05	0.02	(0.09)	(0.30)
Loss from the cumulative effect of a change in accounting policy per share	—	—	—	(1.93)
Basic earnings (loss) per share	\$ 0.09	\$ (0.47)	\$ (1.30)	\$ (2.91)
Diluted earnings (loss) per share	\$ 0.09	\$ (0.47)	\$ (1.30)	\$ (2.91)
Weighted average number of shares used in the calculation of earnings (loss) per share:				
Basic	28.7	28.7	28.7	28.7
Diluted	28.7	28.7	28.7	28.7

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Consolidated Statement of Operations Data (continued):

(in millions, except per share amounts)

- (a) During fiscal years 2001 and 2002, in response to excess capacity caused by slowing technology end markets, the Company commenced restructuring programs aimed at reducing its cost structure. During the three and nine months ended September 28, 2003, the Company recorded additional restructuring charges resulting from the 2001 and 2002 restructuring programs of \$3.6 million and \$4.3 million, respectively, related to lease and other contract obligations, severance, asset impairment charges and other facility exit costs and other charges of \$0.6 million and \$0.9 million, respectively, related to professional fees of \$0.6 million associated with the Company's refinancing negotiations with current and potential lenders and investors and a discount of \$0.3 million on the settlement of shareholder loans. Also, during the three and nine months ended September 28, 2003, the Company recorded adjustments to its initial 2001 and 2002 restructuring plans of \$4.2 million and \$5.3 million, respectively, due to the Company settling certain obligations for less than the original estimated amounts and due to the Company receiving proceeds on assets previously written off. Refer to note 8 to our consolidated financial statements.
- (b) During the second quarter of 2003 the Company performed its quarterly review of its deferred tax assets in accordance with SFAS No. 109. This review resulted in a decision to establish a full valuation allowance of for its deferred tax assets. Refer to note 6 to our consolidated financial statements.
- (c) During the third quarter of 2003 the Company sold the manufacturing operations of the Appleton facility for proceeds of \$3.1 million. The Company recorded a restructuring charge of \$3.2 million reflecting the write-down of the Appleton assets to the estimated realizable value during the second quarter of 2003 and a loss on disposition of \$0.2 million in the third quarter of 2003. Refer to note 9 to our consolidated financial statements.

In February, 2002 the main customer of the Cork, Ireland facility was placed into administration as part of a financial restructuring. As a result, on March 19, 2002, the Company announced that it was closing the Cork, Ireland facility and that it was taking steps to place the subsidiary that operated that facility in voluntary administration. During the third quarter of 2003, the Company received a distribution from the proceeds of the liquidation of \$2.3 million and recorded additional changes of \$0.7 million related to the wind-down of the facility and related operations. Refer to note 9 to our consolidated financial statements.

- (d) During 2002, the Company completed its transitional goodwill impairment test resulting in a goodwill impairment charge of \$55.6 million. Prior to January 1, 2002, goodwill was amortized on a straight-line basis over 10 years. Effective January 1, 2002, the Company discontinued amortization of all existing goodwill as a result of a new accounting standard issued in 2001. Refer to note 10 to our consolidated financial statements.

Consolidated Balance Sheet Data:

(in millions)

	September 28, 2003 (Unaudited)	December 31, 2002
Cash	\$ 0.6	\$ 0.4
Working capital (deficiency)	5.6	(8.2)
Total assets	126.7	191.0
Total debt, including current maturities	74.9	82.6
Shareholders' equity (deficit)	(19.0)	18.0

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Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

We provide advanced electronics manufacturing services, or EMS, to electronics industry original equipment manufacturers, or OEMs, primarily in the networking, industrial and communications market segments. We currently service our customers through four manufacturing and technology centers strategically located in key technology corridors in the United States, Canada and the cost-effective location of Mexico. Our full range of value-added supply chain services include product design, procurement, prototyping, advanced cable and harness interconnect, high-precision enclosures, printed circuit board assembly, test, final system build, comprehensive supply chain management, packaging, global distribution and after sales support.

During fiscal year 2001, in response to excess capacity caused by slowing technology end markets, we commenced a restructuring program aimed at reducing our cost structure. Actions taken by management to improve capacity utilization included closing our Denver, Colorado assembly facility and our Haverhill, Massachusetts interconnect facility, re-sizing our Mexico and Ireland facilities and addressing our excess equipment capacity. Accordingly, we recorded restructuring charges of \$67.2 million pre-tax (consisting of a write-down of goodwill and other intangible assets and the costs associated with exiting or re-sizing facilities) and other charges of \$27.2 million pre-tax (consisting of accounts receivable, inventory and asset impairment charges).

In response to the continuing industry economic downturn in 2002, the Company took further steps to realign its cost structure and plant capacity. In February, 2002 the main customer of our Cork, Ireland facility was placed into administration as part of a financial restructuring. As a result, on March 19, 2002, we announced that we were closing our Cork, Ireland facility and that we were taking steps to place the subsidiary that operated that facility in voluntary administration. During the first quarter of 2002, we recorded a charge of \$9.7 million related to the closure of the Cork facility, which is included in the loss for discontinued operations. Prior to taking steps to place the subsidiary that operated the Cork facility in voluntary liquidation, we and our lending group executed an amendment to our credit facility to waive the default that would have been caused by this action and amend the agreement to permit such facility closure. During the third quarter of 2003, the Company received a distribution from the proceeds of the liquidation of \$2.3 million and recorded additional charges of \$0.7 million related to the wind-down of the facility and related operations.

In early 2003, we concluded that operations at our Austin, Texas location were not cost competitive and we ceased manufacturing at our Austin site during the first quarter of 2003. We also made the decision to close our interconnect facility in Donegal, Ireland, primarily due to customer losses and reduced volume with existing customers. We ceased manufacturing at our Donegal site during the second quarter of 2003. The Company also initiated the closure of its Charlotte, North Carolina facility during the second quarter of 2003, which corresponded to the expiration of the facility lease and ceased manufacturing at the site at the end of the second quarter of 2003.

During the third and fourth quarters of 2002, the Company recorded restructuring charges of \$37.4 million related the cost of exiting the Donegal and Austin facilities and right-sizing the San Jose, California, Charlotte, North Carolina, Chihuahua, Mexico and Markham, Ontario facilities, including the cost of exiting equipment leases and facility leases, severance costs, asset impairment charges and inventory exposures. Other charges of \$2.1 million were incurred during the third and fourth quarter of 2002 related to inventory charges resulting from the disengagement of a major customer, coupled with the effects of the continued downturn in the technology sector.

The Company recorded additional restructuring and other charges related to the 2001 and 2002 restructuring programs of \$4.3 million during the first nine months of 2003, related to lease and other contract obligations, severance and other facility exit costs as it completes the final stages of the restructuring initiatives and recorded adjustments to its initial 2001 and 2002 restructuring plans of \$5.3 million as it settles certain obligations for less than the original estimated amounts. The Company recorded other charges of \$0.9 million related to the settlement of shareholder loans of \$0.3 million and professional fees of \$0.6 million associated with the current and potential lenders and investors. Also during the third quarter of 2003, the Company sold the manufacturing operations of the Appleton facility for proceeds of \$3.1 million,

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Management has been reviewing the valuation of its assets, and in particular, in assessing the realization of deferred tax assets, management considers whether it is more likely than not that some portion or all of its deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income. Management considers the scheduled reversal of deferred tax liabilities, change of control limitations, projected future taxable income and tax planning strategies in making this assessment. FAS 109 states that forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence such as cumulative losses in recent years in the jurisdictions to which the deferred tax asset relate. As a result of the quarterly review undertaken at the end of the second quarter, the Company concluded that given the weakness and uncertainty in the current economic environment, it was appropriate to establish a full valuation allowance for the deferred tax assets arising from its operations in the jurisdictions to which the deferred tax assets relate. In addition, the Company expects to provide a full valuation allowance on future tax benefits until it can demonstrate a sustained level of profitability that establishes its ability to utilize the assets in jurisdictions to which the assets relate.

As a result of restructuring actions and market conditions we incurred a significant operating loss during 2001, which resulted in our non-compliance with certain financial covenants contained in our credit agreement as at September 30, 2001. The Company and its lenders entered into a term sheet under which the Company operated until February 2002, when we and our lending group executed an amendment to our credit facility to waive the September 30, 2001 defaults and to revise the covenant tests to be consistent with both then-current revenues and the forecast for 2002.

The Company and its lending group agreed in April 2002 to further amend the credit agreement to increase the Company's permitted loan balances to correspond to its higher working capital needs.

The Company and its lending group further amended the credit agreement effective as of December 31, 2002, which was prior to the date on which the Company was to revert back to the covenants under the original credit agreement, to revise certain covenants and waive certain defaults under the credit agreement. The revised terms of the credit agreement establish amended financial and other covenants covering the period up to June 30, 2004, based on the Company's December 2002 business plan.

During November, 2003, the Company and its lending group executed a further amendment to the credit agreement with an effective date of November 17, 2003 (the "Effective Date") providing for a waiver of certain events of default, if any, arising prior to the Effective Date. The Company and its lending group also amended the credit facility to provide for term loans of \$11.9 million and revolving credit loans, swing-line loans and letters of credit of \$80.0 million with an extension of the maturity date to October 1, 2004 and amendments of certain financial and other covenants based on the Company's current business plan. The Company was in compliance with the financial covenants at September 28, 2003. Continued compliance with the amended financial covenants through to October 1, 2004 is dependent on the Company achieving the forecasts inherent in its current business plan. The Company believes the forecasts are based on reasonable assumptions; however, the forecasts are dependent on a number of factors, some of which are outside the control of the Company. These include, but are not limited to, general economic conditions and specifically the strength of the electronics industry and the related demand for the products and services by the Company's customers. In the event of non-compliance, the Company's lenders have the right to demand repayment of all outstanding amounts under the amended credit facility. If we were unable to repay such amounts, the lenders could proceed against any collateral granted to them to secure the indebtedness. Substantially all of the Company's assets have been pledged to the lenders as collateral for the Company's obligations under the senior credit facility.

The Company's revolving credit facility matures on October 1, 2004 and accordingly as at September 28, 2003, this amount has been classified as a long-term liability. The Company has initiatives underway to refinance its bank indebtedness including discussions with current and potential lenders and investors. A transaction resulting from these discussions is likely to involve significant dilution to existing shareholders. To date no agreements have been reached and there can be no assurances that any agreement will be reached. Should the Company not be able to refinance the debt prior to October 1, 2004, the Company expects that it will be unable to repay the full amount of the debt upon maturity. In that event, or in the event of any earlier default under the credit agreement, the Company would attempt to negotiate with its current lenders to modify the terms of the credit agreement. There can be no assurances that the Company will be able to negotiate or reach an agreement with its current lenders to modify the terms of the credit agreement. (See "Liquidity and Capital Resources")

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Corporate History

SMTC Corporation is the result of the July 1999 combination of the former SMTC Corporation, or Surface Mount, and HTM Holdings, Inc., or HTM. Surface Mount was established in Toronto, Ontario in 1985. HTM was established in Denver, Colorado in 1990. SMTC was established in Delaware in 1998. After the combination, we purchased Zenith Electronics' facility in Chihuahua, Mexico, which expanded our cost-effective manufacturing capabilities in an important geographic region. In September 1999, we established a manufacturing presence in the Northeastern United States and expanded our value-added services to include high precision enclosure capabilities by acquiring Boston, Massachusetts based W.F. Wood. In July 2000, we acquired Pensar Corporation, an EMS company specializing in design engineering and headquartered in Appleton, Wisconsin. In November 2000, we acquired Qualtron Teoranta, a provider of specialized cable and harness interconnect assemblies, based in Donegal, Ireland and with a subsidiary in Haverhill, Massachusetts.

On July 27, 2000, we consummated an initial public offering of 6,625,000 shares of our common stock and 4,375,000 exchangeable shares of our subsidiary SMTC Manufacturing Corporation of Canada, or SMTC Canada. Each exchangeable share of SMTC Canada is exchangeable at the option of the holder at any time into one share of our common stock, subject to compliance with applicable securities laws. On August 18, 2000, we sold an additional 1,650,000 shares of common stock upon exercise of the underwriters' over-allotment option.

Results of Operations

We currently provide turnkey manufacturing services to the majority of our customers. Turnkey manufacturing services typically result in higher revenue and higher gross profits but lower gross profit margins when compared to consignment services.

Our contractual arrangements with our key customers generally provide a framework for our overall relationship with our customer. Revenue is recognized upon shipment to the customer as performance has occurred, all customer specified acceptance criteria have been tested and met, and the earnings process is considered complete. Actual production volumes are based on purchase orders for the delivery of products. Typically, these orders do not commit to firm production schedules for more than 30 to 90 days in advance. In order to minimize inventory risk, we generally order materials and components only to the extent necessary to satisfy existing customer forecasts or purchase orders. Fluctuations in material costs typically are passed through to customers. We may agree, upon request from our customers, to temporarily delay shipments, which causes a corresponding delay in our revenue recognition.

Our fiscal year end is December 31. The consolidated financial statements of SMTC are prepared in accordance with United States GAAP.

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The following table sets forth certain operating data expressed as a percentage of revenue for the periods ended:

(Unaudited)

	Three months ended		Nine months ended	
	September 28, 2003	September 29, 2002 (Restated)	September 28, 2003	September 29, 2002 (Restated)
Revenue	100.0%	100.0%	100.0%	100.0%
Cost of sales, including restructuring and other charges	89.4	99.3	90.9	97.1
Gross profit	10.6	0.7	9.1	2.9
Selling, general and administrative expenses	6.0	4.2	6.1	4.3
Amortization	1.2	0.5	1.3	0.4
Restructuring and other charges	—	4.4	—	1.6
Operating income (loss)	3.4	(8.4)	1.7	(3.4)
Interest	1.4	1.3	1.7	1.6
Earnings (loss) before income taxes, discontinued operations and the cumulative effect of a change in accounting policy	2.0	(9.7)	—	(5.0)
Income tax expense (recovery)	0.3	0.0	15.2	(0.3)
Earnings (loss) from continuing operations	1.7	(9.7)	(15.2)	(4.7)
Earnings (loss) from discontinued operations	1.7	0.4	(1.0)	(2.0)
Cumulative effect of a change in accounting policy	—	—	—	(13.4)
Net earnings (loss)	3.4%	(9.3)%	(16.2)%	(20.1)%

Quarter ended September 28, 2003 compared to the quarter ended September 29, 2002

Revenue

Revenue decreased \$66.5 million, or 46.3%, from \$143.5 million in the third quarter of 2002 to \$77.0 million in the third quarter of 2003 due to the Company's decision to terminate its supply agreement with Dell during 2002 and to a reduction in revenue earned from IBM, Alcatel and other customers due to the continued economic slowdown in the technology sector. During the second quarter of 2002, the Company informed Dell of its intention to terminate its supply agreement and to end production over the third quarter of 2002. The Company's decision was taken after a review of the Company's return on capital requirements indicated that the customer's programs were not generating sufficient returns and, at the same time, were utilizing a disproportionate amount of working capital.

During the third quarter of 2003, we recorded approximately \$2.0 million of sales of raw materials inventory to customers, which carried no margin, compared to \$8.3 million of such sales for the same period in 2002.

Revenue from the IBM program of \$20.7 million, Ingenico of \$15.3 million and Square D (a division of Schneider Electric) of \$8.1 million for the third quarter of 2003 was 26.9%, 19.8% and 10.6%, respectively, of total revenue for the period. Revenue from Dell of \$32.6 million, IBM of \$28.8 million and Alcatel of \$17.2 million for the third quarter of 2002 was 22.7%, 20.0% and 12.0%, respectively, of total revenue for the period. No other customers represented more than 10% of revenue in either period.

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In the third quarter of 2003, 58.7% of our revenue was generated from operations in Mexico, 22.0% from the United States and 19.3% from Canada. In the third quarter of 2002, 47.6% of our revenue was generated from operations in the United States, 36.0% from Mexico, 15.7% from Canada, and 0.7% from Europe. We expect to continue to increase the portion of revenue attributable to our Chihuahua and Markham facilities, with the transfer of certain production from other facilities. We terminated manufacturing in Europe during the second quarter of 2003.

Gross Profit

Gross profit increased \$7.3 million from \$0.9 million, or 0.7% of revenue, for the third quarter of 2002 to \$8.2 million, or 10.6% of revenue, for the third quarter of 2003. Gross profit for the third quarter of 2002 includes the effect of restructuring charges of \$6.3 million related to an additional write-down of inventory in connection with the closure of the Denver facility and other inventory related charges of \$0.9 million resulting from the costs associated with the disengagement of Dell. Excluding restructuring and other charges, gross profit increased \$0.1 million from \$8.1 million, or 5.6 % of revenue, for the third quarter of 2002 to \$8.2 million, or 10.6% of revenue, for the third quarter of 2003. The improvement of gross profit margin, excluding restructuring and other charges, is due to a change in customer mix as the Company continues to diversify its customer base coupled with improved manufacturing and supply chain efficiencies resulting from the operational restructuring and rationalization programs initiated in 2001 and 2002.

The Company writes down estimated obsolete or excess inventory for the difference between the cost of inventory and estimated market value based upon customer forecasts, shrinkage, the aging and future demand of the inventory, past experience with specific customers and the ability to sell back inventory to customers or suppliers. If these estimates change, additional write-downs may be required.

Selling, General & Administrative Expenses

Selling, general and administrative expenses decreased \$1.4 million from \$6.0 million, or 4.2% of revenue, for the third quarter of 2002 to \$4.6 million, or 6.0% of revenue, for the third quarter of 2003. The reduction in selling, general and administrative expenses is due to the closure of our Donegal, Austin and Charlotte facilities and to our continued focus on reducing selling, general and administrative expenses at each operating site. The increase in selling, general and administrative expenses as a percentage of revenue is a result of the lower sales base.

Amortization

Amortization of intangible assets of \$1.0 million for the third quarter of 2003 represents the amortization of deferred finance costs related to the establishment of our senior credit facility in July 2000 and subsequent amendments. The costs associated with our amended and restated senior credit facility are being amortized over the remaining term of the debt.

Amortization of intangible assets of \$0.6 million for the third quarter of 2002 included the amortization of \$0.5 million of deferred finance costs related to the establishment of our senior credit facility in July 2000 and subsequent amendments, and \$0.1 million of deferred equipment lease costs.

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Restructuring and Other Charges

The following table relates to the components of the restructuring and other charges for the three months ended September 28, 2003 and September 29, 2002:

	Three months ended	
	September 28, 2003	September 29, 2002
(in millions)		
Inventory write-downs included in cost of sales	\$ —	\$ 6.3
Lease and other contract obligations	2.4	5.8
Adjustments of previously recorded lease and other contract obligations	(3.5)	(0.4)
Severance	1.1	1.0
Other facility exit costs	0.1	—
Adjustments to other facility exit costs	(0.6)	—
Asset impairment	0.0	—
Proceeds on assets previously written down	(0.1)	—
	<u>(0.6)</u>	<u>6.4</u>
	(0.6)	12.7
Other charges included in restructuring and other charges	0.6	—
Other charges included in cost of sales	—	0.9
	<u>\$ 0.0</u>	<u>\$ 13.6</u>

2001 Restructuring Plan:

During fiscal year 2001, in response to excess capacity caused by slowing technology end markets, the Company commenced a restructuring program aimed at reducing its cost structure.

During the third quarter of 2003, the Company recorded additional lease and other contract obligations of \$2.2 million related to the costs associated the facility lease in Monterrey, Mexico. Also, during the third quarter of 2003, the Company recorded an adjustment to its initial 2001 restructuring plan of \$0.2 million due to the Company settling certain obligations for less than the original estimated amounts.

2002 Restructuring Plan:

In response to the continuing industry economic downturn, the Company took further steps to realign its cost structure and plant capacity and in the third and fourth quarter of 2002 recorded restructuring charges of \$37.4 million related to the cost of exiting equipment and facility leases, severance costs, asset impairment charges, inventory exposures and other facility exit costs and other charges of \$2.1 million primarily related to the costs associated with the disengagement of a customer and the continued downturn.

During the third quarter of 2003, the Company recorded additional restructuring charges of \$1.4 million related to the 2002 restructuring plan. Lease and other contract obligations of \$0.2 million relate to additional costs associated with idling equipment leases at the Donegal facility. Severance costs of \$1.1 million recorded during the third quarter of 2003 include \$0.9 million related to the closure of the Charlotte facility and the resizing of other facilities. The severance costs relate to 96 plant and operational employees, primarily at the

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Charlotte facility. Other facility costs of \$0.1 million relate largely to costs associated with closing the Charlotte facility

Also during the third quarter of 2003, the Company recorded adjustments to its initial 2002 restructuring plan of \$4.0 million. Adjustments to previously recorded lease and other contract obligations of \$3.5 million and other facility exit costs of \$0.4 million recorded during the third quarter of 2003 relate to the Company revising its original estimates associated with the costs of closing the Austin and Charlotte facilities, based on the settlement of certain liabilities for less than previously estimated and the effects of ongoing negotiations. The Company also recorded a gain of \$0.1 million related to the disposal of assets previously written down at the Donegal facility.

The Company expects the majority of the remaining restructuring accruals as at September 28, 2003 of \$3.1 million relating to the 2001 restructuring program and \$8.5 million relating to the 2002 restructuring program to be paid by the end of fiscal year 2004, with the exception of the accrual related to the Monterrey, Mexico facility, which extends to 2007.

Other charges recorded during the third quarter of 2003 of \$0.6 million relate to professional fees associated with the Company's refinancing negotiations with current and potential lenders and investors.

Interest Expense

Interest expense decreased \$0.8 million from \$1.9 million for the third quarter of 2002 to \$1.1 million, for the third quarter of 2003 due to lower average debt outstanding during the third quarter of 2003 and coupled with lower interest rates. The weighted average interest rates with respect to the debt for the third quarter of 2003 and 2002 were 6.6% and 7.4%, respectively.

Income Tax Expense

In assessing the realization of deferred tax assets, management considers whether it is more likely than not that some portion or all of its deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income. Management considers the scheduled reversal of deferred tax liabilities, change of control limitations, projected future taxable income and tax planning strategies in making this assessment. FAS 109 states that forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence such as cumulative losses in recent years in the jurisdictions to which the deferred tax assets relate. As a result of the quarterly review undertaken at the end of the second quarter, the Company concluded that given the weakness and uncertainty in the current economic environment, it was appropriate to establish a full valuation allowance for the deferred tax assets arising from its operations in the jurisdictions to which the deferred tax assets relate. As a result, the total valuation allowance for deferred tax assets in all jurisdictions worldwide increased from approximately \$35.0 million at December 31, 2002 to approximately \$71.0 million at June 29, 2003, resulting in income tax expense during the quarter ended June 29, 2003, of approximately \$34.2 million. In addition, the valuation allowance as at September 28, 2003 remained at approximately \$71.0 million. The Company expects to provide a full valuation allowance on future tax benefits until it can demonstrate a sustained level of profitability that establishes its ability to utilize the assets in the jurisdictions to which the assets relate.

For the third quarter of 2002, an income tax expense of \$nil was recorded on a pre-tax loss before discontinued operations and the cumulative effect of a change in accounting policy of \$14.0 million, as losses in certain jurisdictions were not tax effected due to the uncertainty of our ability to utilize such losses and the effects of the valuation reserve for the loss carryforwards.

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Discontinued operations

Appleton:

During the third quarter of 2003, the Company sold the manufacturing operations of the Appleton facility for cash proceeds of \$3.1 million. The Appleton facility has historically been included in the results of the United States segment. The Company recorded a restructuring charge of \$3.2 million in the second quarter of 2003 reflecting the write-down of the assets to the estimated realizable value and a loss on disposal of discontinued operation of \$0.2 million in the third quarter of 2003, which has been included in the loss from discontinued operations. Details of the net assets disposed of are as follows:

(in millions)	
Proceeds on disposal	\$ 3.1
Accounts receivable	1.9
Inventory	1.1
Prepaid expenses	0.1
Capital assets	1.7
Accounts payable	(1.4)
Accrued liabilities	(0.5)
Net assets disposed of	2.9
Costs of disposal	0.4
Loss on disposal of discontinued operation	\$ 0.2

The following information included in discontinued operations relates to the Appleton manufacturing operations:

(in millions)	Three months ended	
	September 28, 2003	September 29, 2002
Revenue	\$ 2.5	\$ 9.4
Earnings (loss) from discontinued operations	\$ (0.2)	\$ 0.6

Included in the earnings (loss) from discontinued operations for the three months ended September 28, 2003 is the loss on disposition of discontinued operation of \$0.2 million.

The Company recorded an accrual for closing costs related to the disposition of the Appleton manufacturing operations of \$0.4 million. The remaining accrual at September 28, 2003 relating to the disposition is \$0.3 million.

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Cork:

In February, 2002 the main customer of our Cork, Ireland facility was placed into administration as part of a financial restructuring. As a result, on March 19, 2002, we announced that we were closing our Cork, Ireland facility and that we were taking steps to place the subsidiary that operated that facility in voluntary administration. During the first quarter of 2002, we recorded a charge of \$9.7 million related to the closure of the facility. During the third quarter of 2003 the Company received a distribution from the proceeds of the liquidation of \$2.3 million and recorded additional charges of \$0.7 million related to the wind-down of the facility and related operations.

The following information relates to the Cork discontinued operations:

	Three months ended	
	September 28, 2003	September 29, 2002
(in millions)		
Revenue	\$ —	\$ —
Earnings from discontinued operations	\$ 1.5	\$ —

In 2003, the earnings from discontinued operations include the distribution from the proceeds of the liquidation of \$2.3 million less additional charges of \$0.7 million related to the wind-down of the facility and related operations.

Nine months ended September 28, 2003 compared to the nine months ended September 29, 2002

Revenue

Revenue decreased \$186.9 million, or 44.9%, from \$416.1 million for the first nine months of 2002 to \$229.2 million for the same period in 2003 due to the Company's decision to terminate its supply agreement with Dell during 2002 and to a reduction in revenue earned from IBM, Alcatel and other customers due to the continued economic slowdown in the technology sector. During the second quarter of 2002, the Company informed Dell of its intention to terminate its supply agreement and to end production over the third quarter of 2002. The Company's decision was taken after a review of the Company's return on capital requirements indicated that the customer's programs were not generating sufficient returns and, at the same time, were utilizing a disproportionate amount of working capital.

During the first nine months of 2003, we recorded approximately \$6.3 million of sales of raw materials inventory to customers, which carried no margin, compared to \$25.9 million of such sales for the same period in 2002.

Revenue from the IBM program of \$60.7 million, Ingenico of \$34.0 million and Alcatel of \$23.4 million for first nine months of 2003 was 26.5%, 14.8% and 10.2%, respectively, of total revenue for the period. Revenue from IBM of \$90.7 million, Dell of \$85.0 million and Alcatel of \$53.1 million for the first nine months of 2002 was 21.8%, 20.4% and 12.8%, respectively, of total revenue for the period. No other customers represented more than 10% of revenue in either period.

In the first nine months of 2003, 44.7% of our revenue was generated from operations in Mexico, 32.2% from the United States, 22.1% from Canada and 1.0% from Europe. In the first nine months of 2002, 50.1% of our revenue was generated from operations in the United States, 33.6% from Mexico, 15.4% from Canada, and 0.9% from Europe. We expect to continue to increase the portion of revenue attributable to our Chihuahua and Markham facilities, with the transfer of certain production from other facilities. We terminated manufacturing in Europe during the second quarter of 2003.

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Gross Profit

Gross profit increased \$8.9 million from \$11.9 million, or 2.9% of revenue, for the first nine months of 2002 to \$20.8 million, or 9.1% of revenue, for the same period in 2003. Gross profit for the first nine months of 2002 includes the effect of restructuring charges of \$6.3 million related to an additional write-down of inventory in connection with the closure of the Denver facility and other inventory related charges of \$0.9 million resulting from the costs associated with the disengagement of Dell. Excluding restructuring and other charges, gross profit increased \$1.7 million from \$19.1 million, or 4.6 % of revenue, for the first nine months of 2002 to \$20.8 million, or 9.1% of revenue, for the third quarter of 2003. The improvement of gross profit margin, excluding restructuring and other charges, is due to a change in customer mix as the Company continues to diversify its customer base coupled with improved manufacturing and supply chain efficiencies resulting from the operational restructuring and rationalization programs initiated in 2001 and 2002.

The Company writes down estimated obsolete or excess inventory for the difference between the cost of inventory and estimated market value based upon customer forecasts, shrinkage, the aging and future demand of the inventory, past experience with specific customers and the ability to sell back inventory to customers or suppliers. If these estimates change, additional write-downs may be required.

Selling, General & Administrative Expenses

Selling, general and administrative expenses decreased \$4.0 million from \$18.0 million, or 4.3% of revenue, for the first nine months of 2002 to \$14.0 million, or 6.1% of revenue, for the same period in 2003. The reduction in selling, general and administrative expenses is a result of closing our Austin, Charlotte and Donegal facilities and our continued focus on reducing selling, general and administrative expenses at each operating site. The increase in selling, general and administrative expenses as a percentage of revenue is a result of the lower sales base.

Amortization

Amortization of intangible assets of \$2.9 million for the first nine months of 2003 represents the amortization of deferred finance costs related to the establishment of our senior credit facility in July 2000 and subsequent amendments. The costs associated with our amended and restated senior credit facility are being amortized over the remaining term of the debt.

Amortization of intangible assets of \$1.7 million for the first nine months of 2002 included the amortization of \$1.5 million of deferred finance costs related to the establishment of our senior credit facility in July 2000 and subsequent amendments, and \$0.2 million of deferred equipment lease costs.

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Restructuring and Other Charges

The following table relates to the components of the restructuring and other charges for the nine months ended September 28, 2003 and September 29, 2002:

	Nine months ended	
	September 28, 2003	September 29, 2002
(in millions)		
Inventory write-downs included in cost of sales	\$ —	\$ 6.3
Lease and other contract obligations	2.5	5.8
Adjustments of previously recorded lease and other contract obligations	(4.1)	(0.4)
Severance	1.7	1.0
Other facility exit costs	0.1	—
Adjustments to other facility exit costs	(0.9)	—
Asset impairment	0.0	—
Proceeds on assets previously written down	(0.3)	—
	<u>(1.0)</u>	<u>6.4</u>
	(1.0)	12.7
Other charges included in restructuring and other charges	0.9	—
Other charges included in cost of sales	—	0.9
	<u>\$ (0.1)</u>	<u>\$ 13.6</u>

2001 Restructuring Plan:

During fiscal year 2001, in response to excess capacity caused by slowing technology end markets, the Company commenced a restructuring program aimed at reducing its cost structure.

During the first nine months of 2003, the Company recorded additional lease and other contract obligations of \$2.2 million related to the costs associated with the facility lease in Monterrey, Mexico. Also, during the first nine months of 2003, the Company recorded an adjustment to its initial 2001 restructuring plan of \$0.2 million due to the Company settling certain obligations for less than the original estimated amounts.

2002 Restructuring Plan:

In response to the continuing industry economic downturn, the Company took further steps to realign its cost structure and plant capacity and in the third and fourth quarter of 2002 recorded restructuring charges of \$37.4 million related to the cost of exiting equipment and facility leases, severance costs, asset impairment charges, inventory exposures and other facility exit costs and other charges of \$2.1 million primarily related to the costs associated with the disengagement of a customer and the continued downturn.

During the first nine months of 2003, the Company recorded additional restructuring charges of \$2.1 million and other charges of \$0.9 million related to the 2002 restructuring plan. Lease and other contract obligations of \$0.3 million relate to additional costs associated with idling equipment leases at the Donegal facility. Severance costs of \$1.7 million recorded during the nine months include \$1.4 million related to the closure of the Austin and Charlotte facilities and the resizing of other facilities. The severance costs relate to 206 plant and operational employees, primarily at the Austin, Charlotte and Mexico facilities. Other facility costs of \$0.1 million relate largely to costs associated with closing the Charlotte facility.

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Also during the first nine months of 2003, the Company recorded adjustments to its initial 2002 restructuring plan of \$5.1 million. Adjustments to previously recorded lease and other contract obligations of \$4.1 million and other facility exit costs of \$0.7 million recorded during the first nine months of 2003 relate to the Company revising its original estimates associated with the costs of closing the Austin and Charlotte facilities, based on the settlement of certain liabilities for less than previously estimated and the effects of ongoing negotiations. The Company also recorded a gain of \$0.3 million related to the disposal of assets previously written down at the Donegal and Austin facilities.

The Company expects the majority of the remaining restructuring accruals as at September 28, 2003 of \$3.1 million relating to the 2001 restructuring program and \$8.5 million relating to the 2002 restructuring program to be paid by the end of fiscal year 2004, with the exception of the accrual related to the Monterray, Mexico facility, which extends to 2007.

Other charges recorded during the first nine months of 2003 of \$1.0 million include \$0.6 million related to professional fees associated with the Company's refinancing negotiations with current and potential lenders and investors. In light of the Company's plan to lower its bank indebtedness, it requested that certain shareholder loans be repaid prior to the expiration of the term. Accordingly, during the second quarter of 2003 the Company recorded a discount of \$0.4 million on the prepayment of shareholder loans that had a carrying value of \$4.2 million, resulting in net proceeds of \$3.8 million.

Interest Expense

Interest expense decreased \$2.7 million from \$6.6 million for the first nine months of 2002 to \$3.9 million for the same period in 2003 due to lower average debt outstanding during the first nine months of 2003, coupled with lower interest rates. The weighted average interest rates with respect to the debt for the first nine months of 2003 and 2002 were 6.6% and 7.2%, respectively.

Income Tax Expense

In assessing the realization of deferred tax assets, management considers whether it is more likely than not that some portion or all of its deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income. Management considers the scheduled reversal of deferred tax liabilities, change of control limitations, projected future taxable income and tax planning strategies in making this assessment. FAS 109 states that forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence such as cumulative losses in recent years in the jurisdictions to which the deferred tax assets relate. As a result of the quarterly review undertaken at the end of the second quarter, the Company concluded that given the weakness and uncertainty in the current economic environment, it was appropriate to establish a full valuation allowance for the deferred tax assets arising from its operations in the jurisdictions to which the deferred tax assets relate. As a result, the total valuation allowance for deferred tax assets in all jurisdictions worldwide increased from approximately \$35.0 million at December 31, 2002 to approximately \$71.0 million at June 29, 2003, resulting in income tax expense during the quarter ended June 29, 2003, of approximately \$34.2 million. In addition, the valuation allowance at September 28, 2003 remained at approximately \$71.0 million. The Company expects to provide a full valuation allowance on future tax benefits until it can demonstrate a sustained level of profitability that establishes its ability to utilize the assets in the jurisdictions to which the assets relate.

For the nine months ended September 29, 2002, an income tax recovery of \$1.3 million was recorded on a pre-tax loss before discontinued operations of \$5.3 million resulting in an effective tax recovery rate of 18.9%, as losses in certain jurisdictions were not tax effected due to the uncertainty of our ability to utilize such losses.

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Discontinued Operations

Appleton:

During the third quarter of 2003, the Company sold the manufacturing operations of the Appleton facility for cash proceeds of \$3.1 million. The Appleton facility has historically been included in the results of the United States segment. The Company recorded a restructuring charge of \$3.2 million in the second quarter of 2003 reflecting the write-down of the assets to the estimated realizable value and a loss on disposal of discontinued operation of \$0.2 million in the third quarter of 2003, which has been included in the loss from discontinued operations. Details of the net assets disposed of are as follows:

<i>(in millions)</i>	
Proceeds on disposal	\$ 3.1
Accounts receivable	1.9
Inventory	1.1
Prepaid expenses	0.1
Capital assets	1.7
Accounts payable	(1.4)
Accrued liabilities	(0.5)
Net assets disposed of	2.9
Costs of disposal	0.4
Loss on disposal of discontinued operation	\$ 0.2

The following information included in discontinued operations relates to the sale of the Appleton manufacturing operations:

<i>(in millions)</i>	Nine months ended	
	September 28, 2003	September 29, 2002
Revenue	\$ 10.8	\$ 37.4
Earnings (loss) from discontinued operations	\$ (4.0)	\$ 1.8

Included in the earnings (loss) from discontinued operations for the nine months ended September 28, 2003 is the loss on disposition of discontinued operation of \$0.2 million, a restructuring charge of \$3.2 million reflecting the write-down of the Appleton assets to the estimated realizable value and the loss from operations of \$0.5 million.

The Company recorded an accrual for closing costs related to the disposition of the Appleton manufacturing operations of \$0.4 million. The remaining accrual at September 28, 2003 relating to the disposition is \$0.3 million.

Cork:

In February, 2002 the main customer of our Cork, Ireland facility was placed into administration as part of a financial restructuring. As a result, on March 19, 2002, we announced that we were closing our Cork, Ireland facility and that we were taking steps to place the subsidiary that operated that facility in voluntary administration. During the first quarter of 2002, we recorded a charge of \$9.7 million related to the closure of the facility. During the third quarter of 2003 the Company received a distribution from the proceeds of the

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liquidation of \$2.3 million and recorded additional charges of \$0.7 million related to the wind-down of the facility and related operations. The following information relates to the discontinued operations:

(in millions)	Nine months ended	
	September 28, 2003	September 29, 2002
Revenue	\$ —	\$ 5.0
Earnings (loss) from discontinued operations	\$ 1.6	\$ (10.2)

For the nine months ended September 28, 2003, the earnings from discontinued operations include the distribution from the proceeds of the liquidation of \$2.3 million less additional charges of \$0.7 million related to the wind-down of the facility and related operations.

For the nine months ended September 29, 2002, the loss from discontinued operations includes the cost of closing the Cork facility of \$9.7 million. Within this amount are the write-off of the net assets of \$6.7 million (comprised of capital assets of \$1.1 million and net working capital of \$5.6 million) and other costs associated with exiting the facility of \$3.0 million. Included in the other costs is severance of \$1.3 million related to the termination of all employees at that site.

Costs of \$2.7 million were paid out during 2002 and costs of \$0.2 million were paid out during the nine months ended September 28, 2003, leaving an accrual of \$0.7 million at the end of the third quarter of 2003.

Liquidity and Capital Resources

Our principal sources of liquidity are cash provided from operations and borrowings under our senior credit facility. In the past, we have also relied on our access to the capital markets. Our principal uses of cash have been to meet debt service requirements, to finance capital expenditures and working capital requirements and to fund operating losses in certain periods. We anticipate our principal uses of cash in the future will continue to be to meet debt service requirements and to finance capital expenditures and working capital requirements.

During November, 2003, the Company and its lending group executed an amendment to the credit agreement with an effective date of November 17, 2003 (the "Effective Date"), providing for a waiver of certain events of default, if any, arising prior to the Effective Date. The Company and its lending group also amended the credit facility to provide for term loans of \$11.9 million and revolving credit loans, swing-line loans and letters of credit of \$80.0 million with an extension of the maturity date to October 1, 2004 and amendments of certain financial and other covenants based on the Company's current business plan. The Company was in compliance with the financial covenants at September 28, 2003. Continued compliance with the amended financial covenants through to October 1, 2004 is dependent on the Company achieving the forecasts inherent in its current business plan. The Company believes the forecasts are based on reasonable assumptions and are achievable; however, the forecasts are dependent on a number of factors, some of which are outside the control of the Company. These include, but are not limited to, general economic conditions and specifically the strength of the electronics industry and the related demand for the products and services by the Company's customers. In the event of non-compliance, the Company's lenders will have the right to demand repayment of all outstanding amounts under the amended credit facility. If we were unable to repay such amounts, the lenders could proceed against any collateral granted to them to secure the indebtedness. Substantially all of the Company's assets have been pledged to the lenders as collateral for the Company's obligations under the senior credit facility.

The Company's revolving credit facility matures on October 1, 2004 and accordingly as at September 28, 2003, this amount has been classified as a long-term liability. The Company has initiatives underway to refinance its bank indebtedness including discussions with current and potential lenders and investors. A transaction resulting from these discussions is likely to involve significant dilution to existing shareholders. To date no agreements have been reached and there can be no assurances that any agreement will be reached. Should the Company not be able to refinance the debt prior to October 1, 2004, the Company expects that it will

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be unable to repay the full amount of the debt upon maturity. In that event, or in the event of any earlier default under the credit agreements, the Company would attempt to negotiate with its current lenders to modify the terms of the credit agreement. There can be no assurances that the Company will be able to negotiate or reach an agreement with its current lenders to modify the terms of the credit agreement.

During the second quarter of 2002, the Company informed Dell of its intention to terminate its supply agreement with Dell and to end production over the third quarter of 2002. The Company's decision was taken after a review of the Company's return on capital requirements indicated that the customer's programs were not generating sufficient returns and, at the same time, were utilizing a disproportionate amount of working capital.

Nine months ended September 28, 2003 Liquidity:

Net cash provided by operating activities for the first nine months of 2003 was \$1.0 million. Cash was generated largely from the operating loss of \$37.2 million, after adjusting for non cash items of \$47.3 million, the collection of accounts receivable and a reduction in inventory, partially offset by a decline in accounts payable and accrued liabilities.

Net cash used in financing activities for the first nine months of 2003 was \$4.0 million due to the net repayment of long-term debt of \$7.7 million and the repayment of capital leases of \$0.1 million, partially offset by the repayment of shareholder loans of \$3.8 million.

Net cash provided by investing activities for the first nine months of 2003 was \$3.3 million, largely the result of proceeds from the disposition of the Appleton facility and manufacturing operations of \$3.1 million and from the sale of capital assets of \$0.3 million, offset by the purchase of capital assets of \$0.1 million.

Nine months ended September 29, 2002 Liquidity:

Net cash provided by operating activities for the first nine months of 2002 was \$25.4 million. Cash was generated largely by collections of accounts receivable and a reduction in inventory.

Net cash used in financing activities for the nine months ended September 29, 2002 was \$34.8 million due to the repayment of long-term debt of \$32.7 million, the repayment of capital leases of \$0.1 million and the costs associated with the amendment to our credit agreement of \$2.0 million.

Net cash used in investing activities for the nine months ended September 29, 2002 was \$2.1 million due to the purchase of capital assets of \$2.5 million, offset by proceeds from the sale of capital assets of \$0.2 million and other assets of \$0.2 million.

Capital Resources

As a result of restructuring actions and market conditions, we incurred a significant operating loss during 2001, which resulted in our non-compliance with certain financial covenants contained in our credit agreement as at September 30, 2001. The Company and its lenders entered into a term sheet under which the Company operated until February 2002 when we and our lending group executed an amendment to our credit facility to waive the September 30, 2001 defaults and to revise the covenant tests to be consistent with both then-current revenues and the forecast for 2002.

In connection with the February 2002 amendment, the Company agreed to issue to the lenders warrants to purchase common stock of the Company for 1.5% of the total outstanding shares on February 11, 2002 and 0.5% of the total outstanding shares on December 31, 2002. All of these warrants were cancelled in exchange for warrants issued in connection with the December 31, 2002 amendment, as described below.

The Company paid amendment fees of \$1.5 million comprised of \$0.7 million, representing 0.5% of the lender's commitments under the revolving credit facilities and term loans outstanding at February 11, 2002, and other amendment related fees of \$0.8 million.

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In March 2002, we and our lenders executed an amendment to our credit facility to waive the default that would have been caused by placing the subsidiary that operated the Cork, Ireland facility in voluntary liquidation. We paid \$0.1 million in amendment fees in connection with such amendment.

The Company and its lending group agreed in April 2002 to further amend the credit agreement to increase the Company's permitted loan balances to correspond to its higher working capital needs. In connection with such amendment, we paid approximately \$0.1 million in amendment fees.

The Company and its lending group further amended the credit agreement effective December 31, 2002, which was prior to the date on which the Company was to revert back to the covenants under the original credit agreement, to revise certain covenants and waive certain defaults under the credit agreement. The revised terms of the credit agreement established amended financial and other covenants covering the period up to June 30, 2004, based on the Company's December 2002 business plan. The amended facility provided for \$27.5 million in term loans and \$90.0 million in revolving credit loans, swing-line loans and letters of credit.

During November, 2003 the Company and its lending group executed a further amendment to the credit agreement with an effective date of November 17, 2003 (the "Effective Date"), providing for a waiver of certain events of default, if any, arising prior to the Effective Date. The Company and its lending group also amended the credit facility to provide for term loans of \$11.9 million and revolving credit loans, swing-line loans and letters of credit of \$80.0 million with an extension of the maturity date to October 1, 2004 and amendments of certain financial and other covenants based on the Company's current business plan. The Company was in compliance with the financial covenants at September 28, 2003. Continued compliance with the amended financial covenants through to October 1, 2004 is dependent on the Company achieving the forecasts inherent in its current business plan. The Company believes the forecasts are based on reasonable assumptions; however, the forecasts are dependent on a number of factors, some of which are outside the control of the Company. These include, but are not limited to, general economic conditions and specifically the strength of the electronics industry and the related demand for the products and services by the Company's customers. In the event of non-compliance, the Company's lenders have the right to demand repayment of all outstanding amounts under the amended credit facility. If we were unable to repay such amounts, the lenders could proceed against any collateral granted to them to secure the indebtedness. Substantially all of the Company's assets have been pledged to the lenders as collateral for the Company's obligations under the senior credit facility.

The Company's revolving credit facility matures on October 1, 2004 and accordingly as at September 28, 2003, this amount has been classified as a long-term liability. The Company has initiatives underway to refinance its bank indebtedness including discussions with current and potential lenders and investors. A transaction resulting from these discussions is likely to involve significant dilution to existing shareholders. To date no agreements have been reached and there can be no assurances that any agreement will be reached. Should the Company not be able to refinance the debt prior to October 1, 2004, the Company expects that it will be unable to repay the full amount of the debt upon maturity. In that event, or in the event of any earlier default under the credit agreement, the Company would attempt to negotiate with its current lenders to modify the terms of the credit agreement. There can be no assurances that the Company will be able to negotiate or reach an agreement with its current lenders to modify the terms of the credit agreement.

During the amendment period, the facility bears interest at the U.S. base rate as defined in the credit agreement plus 0.25% to 2.5%. As at September 28, 2003 we had borrowed \$74.9 million under this facility.

If the Company is able to achieve its current business plan, management believes that cash generated from operations, available cash and amounts available under our senior credit facility will be adequate to meet our debt service requirements, capital expenditures and working capital needs at our current level of operations and organic growth through October 2004, although no assurance can be given in this regard, particularly with respect to amounts available under our credit facility, as discussed above. If the Company is unable to achieve its current business plan and does not comply with its financial covenants, we would not have sufficient resources to meet our debt service requirements, capital expenditures and working capitals needs unless such default is cured or waived. Further, there can be no assurance that our business will generate sufficient cash flow from operations or that future borrowings will be available to enable us to service our indebtedness. Our future operating performance and ability to service or refinance indebtedness will be subject to future economic conditions and to financial, business and other factors, certain of which are beyond our control.

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In connection with the December 31, 2002 amendment, the lenders returned to the Company for cancellation the existing warrants they held, and the Company agreed to issue to the lenders warrants to purchase common stock of the Company at an exercise price equal to the fair market value (defined as average of the last reported sales price of the common stock of the company for twenty consecutive trading days commencing 22 trading days before the date in question) at the date of the grant for (a) 4.0% of the total outstanding shares on December 31, 2002, (b) 1.0% of the total outstanding shares on December 31, 2002, (c) 0.75% of the total outstanding shares on the date that is 45 days after the end of the Company's first fiscal quarter of 2003, (d) 0.75% of the total outstanding shares on the date that is 45 days after the end of the Company's second fiscal quarter of 2003, (e) 0.75% of the total outstanding shares on the date that is 45 days after the end of the Company's third fiscal quarter of 2003, (f) 0.75% of the total outstanding shares on the date that is 90 days after the end of the Company's fourth fiscal quarter of 2003, (g) 1.0% of the total outstanding shares on the date that is 45 days after the end of the Company's first fiscal quarter of 2004 and (h) 1.0% of the total outstanding shares on the date that is 45 days after the end of the Company's second fiscal quarter of 2004; provided, however that if the Company meets certain EBITDA targets on the dates identified in (c) through (h) above, it will not issue warrants corresponding to such date. The Company met its EBITDA target as at March 30, 2003. As such, the warrants referred to in (c) above were not issued. The Company did not meet its EBITDA target at June 29, 2003 and 228,210 warrants were issued in the third quarter of 2003 with an effective date of August 13, 2003 at an exercise price of \$0.61 per share. Also, the Company did not meet its EBITDA target at September 28, 2003 and will issue 229,934 warrants in the fourth quarter of 2003 with an effective date of November 12, 2003 at an exercise price of \$1.04 per share. If all amounts outstanding under the credit agreement are repaid in full on or before December 31, 2003, all warrants referred to in (b) through (e) above and received by the lenders shall be returned to the Company and cancelled. The warrants will not be tradable separate from the related debt until the later of December 31, 2003 or nine months after the issuance of the warrants being transferred.

In connection with the December 31, 2002 amendment, we paid approximately \$1.7 million in amendment fees. The amendment fees and the fair value of the warrants to be issued in connection with the December 31, 2002 amendment have been accounted for as deferred financing fees included in other assets in the financial statements.

Recently Issued Accounting Standards

In August 2001, the Financial Accounting Standard Board ("FASB") issued Statement No. 143, Accounting for Asset Retirement Obligations, which requires that the fair value of an asset retirement obligation be recorded as a liability, at fair value, in the period in which the Company incurs the obligation. The Statement is effective for fiscal 2003 and there was no material effect as a result of the adoption of this Statement on January 1, 2003.

In July 2002, the FASB issued Statement No. 146, Accounting for Costs Associated with Exit or Disposal Activities ("Statement 146"), which nullifies Emerging Issues Task Force ("EITF") Issue 94-3, Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity ("EITF 94-3"). Statement 146 recognizes the liability for an exit or disposal activity only when a liability is incurred and can be measured at fair value. Under EITF 94-3 a commitment to an exit or disposal plan was sufficient to record the majority of the costs. Statement 146 is effective for exit or disposal activities initiated after December 31, 2002. The Company adopted this Statement on January 1, 2003 and accordingly, the restructuring charges recorded in the first three quarters of 2003 were made in accordance with the new standard.

In November 2002, the FASB issued Interpretation ("FIN") No. 45, Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees and Indebtedness of Others, which requires certain disclosures of obligations under guarantees. The disclosure requirements of FIN 45 were effective for the Company's year ended December 31, 2002. Effective for 2003, FIN 45 also requires the recognition of a liability by a guarantor at the inception of certain guarantees entered into or modified after December 31, 2002, based on the fair value of the guarantee. The Company adopted the disclosure requirements in its 2002 consolidated financial statements. See note 11 for disclosure related to guarantees.

In January 2003, the FASB issued FIN No. 46, Consolidation of Variable Interest Entities, which requires variable interest entities, previously referred to as special-purpose entities or off-balance sheet structures, to be consolidated by a company if that company is subject to a majority of the risk of loss from the entity's activities or is entitled to receive a majority of the entity's returns or both. The consolidation provisions of FIN No. 46 apply immediately to variable interest entities created after January 31, 2003 and to existing entities in the

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first fiscal year or interim period ending after December 15, 2003. Certain disclosure provisions apply in financial statements issued after January 31, 2003. The consolidation requirements of FIN No. 46 are not expected to have a material effect on the Company's consolidated financial statements.

In April 2003, the FASB issued Statement No. 149, Amendments of Statement 133 on Derivative Instruments and Hedging Activities ("Statement 149"), which amends and clarifies financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities under Statement 133. This statement is effective for contracts entered into or modified after June 30, 2003, with certain exceptions, and for hedging relationships designated after June 30, 2003. There was no material effect as a result of the adoption of this statement on July 1, 2003.

In May 2003, the FASB issued Statement No. 150, Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equity ("Statement 150"), which establishes standards for how an issuer classifies and measures certain financial instruments with characteristics of both liabilities and equity. Financial instruments that are within the scope of the statement, which previously were often classified as equity, must now be classified as liabilities. This statement shall be effective for financial instruments entered into or modified after May 31, 2003, and otherwise shall be effective at the beginning of the first interim period after June 15, 2003. There was no material effect as a result of the adoption of this statement in the third quarter of 2003.

Critical Accounting Policies

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

Note 2 to the Consolidated Financial Statements in our Annual Report on Form 10-K for the fiscal year ended December 31, 2002 describes the significant accounting policies and methods used in the preparation of our consolidated financial statements. The following critical accounting policies are impacted significantly by judgments, assumptions and estimates used in the preparation of financial statements. We believe the following critical accounting policies affect our more significant judgments and estimates used in the preparation of our consolidated financial statements.

Income Tax Valuation Allowance

In assessing the realization of deferred tax assets, management considers whether it is more likely than not that some portion or all of its deferred tax assets will not be realized. The ultimate realization of deferred tax assets is dependent upon the generation of future taxable income. Management considers the scheduled reversal of deferred tax liabilities, change of control limitations, projected future taxable income and tax planning strategies in making this assessment. FAS 109 states that forming a conclusion that a valuation allowance is not needed is difficult when there is negative evidence such as cumulative losses in recent years in the jurisdictions to which the deferred tax assets relate. As a result of the quarterly review undertaken at the end of the second quarter, the Company concluded that given the weakness and uncertainty in the current economic environment, it was appropriate to establish a full valuation allowance for the deferred tax assets arising from its operations in the jurisdictions to which the deferred tax assets relate. As a result, in the second quarter of 2003, the total valuation allowance for deferred tax assets in all jurisdictions worldwide increased from approximately \$35.0 million at December 31, 2002 to approximately \$71.0 million at June 29, 2003, resulting in income tax expense during the quarter ended June 29, 2003, of approximately \$34.2 million. In addition, the valuation allowance at September 28, 2003 remained at approximately \$71.0 million. The Company expects to provide a full valuation allowance on future tax benefits until it can demonstrate a sustained level of profitability that establishes its ability to utilize the assets in the jurisdictions to which the assets relate.

Allowance for Doubtful Accounts

The Company evaluates the collectibility of accounts receivable and records an allowance for doubtful accounts, which reduces the accounts receivable to the amount management reasonably believes will be collected. A specific allowance is recorded against customer receivables that are considered to be impaired based on the Company's knowledge of the financial condition of its customers. In determining the amount of the allowance, the Company considers factors including the length of time the receivables have been outstanding, customer and industry concentrations, current business environment and historical experience. Unanticipated changes in the liquidity or financial position of our customers may require additional provisions for doubtful accounts.

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Inventory Valuation

Inventories are valued on a first-in, first-out basis at the lower of cost and replacement cost for raw materials and at the lower of cost and net realizable value for work in progress and finished goods. Inventories include an application of relevant overhead. Our industry is characterized by rapid technological change, short-term customer commitments and rapid changes in demand. The Company writes down estimated obsolete or excess inventory for the difference between the cost of inventory and estimated market value based on customer forecasts, shrinkage, the aging and future demand of the inventory, past experience with specific customers and the ability to sell back inventory to customers or suppliers. If actual market conditions or our customers' product demands are less favorable than those projected, additional provisions may be required.

Restructuring and Other Charges

In response to excess capacity caused by slowing technology end markets, the Company recorded restructuring and other charges aimed at reducing its cost structure. In connection with exit activities, the Company recorded charges for inventory write-downs, employee termination costs, lease and other contractual obligations, long-lived asset impairment and other exit-related costs. These charges were incurred pursuant to formal plans developed by management. The recognition of restructuring and other charges required the Company to make certain judgments and estimates regarding the nature, timing and amount of costs associated with the planned exit activities. The estimates of future liabilities may change, requiring the recording of additional charges or the reduction of liabilities already recorded. At the end of each reporting period, the Company evaluates the remaining accrued balances to ensure that no excess accruals are retained and the utilization of the provision are for their intended purposes in accordance with the developed exit plans.

Long-lived Assets

The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset (or asset groupings) to future net cash flows expected to be generated by the asset. If such assets are considered impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Effective January 1, 2002, the Company adopted the new accounting standard issued in 2001, which is summarized in note 2(q(ii)), changes in accounting policies, to the December 31, 2002 consolidated financial statements contained in our Annual Report on Form 10-K for the year ended December 31, 2002 filed with the Securities and Exchange Commission on March 27, 2003. The adoption of this new accounting standard did not affect the Company's financial statements as at the date of adoption.

FORWARD-LOOKING STATEMENTS

A number of the matters and subject areas discussed in this Form 10-Q are forward-looking in nature. The discussion of such matters and subject areas is qualified by the inherent risks and uncertainties surrounding future expectations generally; these expectations may differ materially from SMTC's actual future experience involving any one or more of such matters and subject areas. SMTC cautions readers that all statements other than statements of historical facts included in this quarterly Form 10-Q regarding SMTC's financial position and business strategy may constitute forward-looking statements. All of these forward-looking statements are based upon estimates and assumptions made by SMTC's management, which although believed to be reasonable, are inherently uncertain. Therefore, undue reliance should not be placed on such estimates and statements. No assurance can be given that any of such estimates or statements will be realized, and it is likely that actual results will differ materially from those contemplated by such forward-looking statements. Factors that may cause such differences include: (1) inability to refinance long-term debt; (2) increased competition; (3) increased costs; (4) the inability to implement our business plan and maintain covenant compliance under our credit agreement; (5) the loss or retirement of key members of management; (6) increases in SMTC's cost of borrowings or lack of availability of debt or equity capital on terms considered reasonable by management; (7) adverse state, federal or foreign legislation or regulation or adverse determinations by regulators; (8) changes in general economic conditions in the markets in which SMTC may compete and fluctuations in demand in the electronics industry; (9) the inability to manage inventory levels efficiently in light of changes in market conditions; and (10) the inability to sustain historical margins as the industry develops. SMTC has attempted to identify certain of the factors that it currently believes may cause actual future experiences to differ from SMTC's current expectations regarding the relevant matter or subject area. In addition to the items specifically discussed in the foregoing,

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SMTC's business and results of operations are subject to the risks and uncertainties described under the heading "Factors That May Affect Future Results" below. The operations and results of SMTC's business may also be subject to the effect of other risks and uncertainties. Such risks and uncertainties include, but are not limited to, items described from time to time in SMTC's reports filed with the Securities and Exchange Commission.

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FACTORS THAT MAY AFFECT FUTURE RESULTS

RISKS RELATED TO OUR CAPITAL STRUCTURE

We need to refinance our credit facility.

The Company's revolving credit facility matures on October 1, 2004. Should the Company not be able to refinance the debt, at the earlier of a covenant violation or the maturity date, the Company expects that it will not be able to satisfy its indebtedness and other obligations. In the event of non-compliance, the Company's lenders have the ability to demand repayment of all outstanding amounts under the credit facility. If the Company was unable to repay such amounts, the lenders could proceed against any collateral granted to them to secure the indebtedness. Substantially all of the Company's assets have been pledged to the lenders as collateral for the Company's obligations under the senior credit facility.

The Company is in the process of pursuing various options with current and potential lenders and investors, however, no agreements with current or potential lenders or investors have been reached yet and there can be no assurance that any agreement will be reached. Any such agreement is likely to involve significant dilution to existing stockholders, which may negatively affect the Company's share price.

We are highly leveraged.

We carry substantially more debt than our competitors. Concerns about our level of debt may adversely affect customers' and suppliers' willingness to do business with us. Furthermore, our level of debt may adversely affect our ability to participate in future growth of the EMS industry and may adversely affect our ability to meet our business plan.

Our indebtedness could adversely affect our financial health and severely limit our ability to plan for or respond to changes in our business.

At September 28, 2003, we had \$74.9 million of indebtedness under our senior credit facility. This debt could have adverse consequences for our business, including:

- We will be more vulnerable to adverse general economic conditions;
- We will be required to dedicate a substantial portion of our cash flow from operations to repayment of debt, limiting the availability of cash for other purposes;
- We may have difficulty obtaining financing in the future for working capital, capital expenditures, acquisitions, general corporate purposes or other purposes;
- We may have limited flexibility in planning for, or reacting to, changes in our business and industry;
- We could be limited by financial and other restrictive covenants in our credit arrangements in our borrowing of additional funds; and
- We may fail to comply with the covenants under which we borrowed our indebtedness which could result in an event of default. If an event of default occurs and is not cured or waived, it could result in all amounts outstanding, together with accrued interest, becoming immediately due and payable. If we were unable to repay such amounts, the lenders could proceed against any collateral granted to them to secure that indebtedness. Substantially all of the Company's assets have been pledged to the lenders as collateral for the Company's obligations under the senior credit facility. In November 2003, the credit agreement was amended to provide financial covenants through October 1, 2004 consistent with our November 2003 business plan. However, there can be no assurance that we will maintain compliance with the covenants under our credit agreement. Continued compliance with the financial covenants is dependent on the Company achieving the forecasts inherent in our business plan. The forecasts are dependent on a number of factors, many of which are outside the control of the Company. These include, but are not limited to, general economic conditions and, specifically, the strength of the electronics industry and the related demand for products and services by the Company's customers. If the

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Company does not comply with its financial covenants and such default is not cured or waived, it could result in all amounts outstanding, together with accrued interest, becoming immediately due and payable.

The Company's revolving credit facility matures in October 2004 and accordingly as at September 28, 2003, this amount has been classified as a long-term liability. The Company has initiatives underway to refinance its bank indebtedness including discussions with current and potential lenders and investors. A transaction resulting from these discussions is likely to involve significant dilution to existing shareholders, which may negatively affect the share price. To date no agreements have been reached and there can be no assurances that any agreement will be reached. Should the Company not be able to refinance the debt prior to October 1, 2004, the Company expects that it will be unable to repay the full amount of the debt upon maturity. In that event, or in the event of any earlier default under the credit agreement, the Company would attempt to negotiate with its current lenders to modify the terms of the credit agreement. There can be no assurances that the Company will be able to negotiate or reach an agreement with its current lenders to modify the terms of the credit agreement.

There can be no assurance that our leverage and such restrictions will not materially adversely affect our ability to finance our future operations or capital needs or to engage in other business activities. In addition, our ability to pay principal and interest on our indebtedness to meet our financial and restrictive covenants and to satisfy our other debt obligations will depend upon our future operating performance, which will be affected by prevailing economic conditions and financial, business and other factors, certain of which are beyond our control, as well as the availability of revolving credit borrowings under our senior credit facility or successor facilities.

The terms of our credit agreement impose significant restrictions on our ability to operate.

The terms of our current credit agreement restrict, among other things, our ability to incur additional indebtedness, complete acquisitions, pay dividends or make certain other restricted payments, consummate certain asset sales, make capital expenditures, incur cash restructuring costs, make timely payments to our suppliers, which may cause credit hold issues, enter into certain transactions with affiliates, merge, consolidate or sell, assign, transfer, lease, convey or otherwise dispose of all or substantially all of our assets. We are also required to maintain specified financial ratios and satisfy certain monthly and quarterly financial condition tests, which further restrict our ability to operate as we choose. During the fourth quarter of 2002, we were in violation of certain covenants contained in our credit agreement. Such violation was waived and the credit agreement was amended to provide financial covenants through June 2004 consistent with our December 2002 business plan. In November 2003, the credit agreement was further amended to provide financial covenants through October 2004 consistent with our November 2003 business plan. As a result of our non-compliance, customers may lose confidence in us and reduce or eliminate their orders with us, which may have a material adverse effect on our business, financial condition and results of operations.

Substantially all of our assets and those of our subsidiaries are pledged as security under our senior credit facility.

Institutional investors have significant influence over our business, and could delay, deter or prevent a change of control or other business combination.

Certain of our institutional investors have representatives on our board of directors, including investment funds affiliated with Bain Capital, LLC and investment funds affiliated with Celerity Partners. By virtue of such stock ownership and board representation, certain of our institutional investors have a significant influence over all matters submitted to our stockholders, including the election of our directors, and exercise significant control over our business policies and affairs. Such concentration of voting power could have the effect of delaying, deterring or preventing a change of control or other business combination that might otherwise be beneficial to our stockholders.

Provisions in our charter documents and state law may make it harder for others to obtain control of us even though some stockholders might consider such a development favorable.

Provisions in our charter, by-laws and certain provisions under Delaware law may have the effect of delaying or preventing a change of control or changes in our management that stockholders consider favorable or

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beneficial. If a change of control or change in management is delayed or prevented, the market price of our shares could suffer.

RISKS RELATED TO OUR BUSINESS AND INDUSTRY

We are exposed to general economic conditions, which could have a material adverse impact on our business, operating results and financial condition.

As a result of recent unfavorable economic conditions and reduced capital spending, our sales have declined from 2001 to 2002 and the first three quarters of 2003. In particular, sales to OEMs in the telecommunications and networking industries worldwide were impacted during 2002 and the first three quarters of 2003. If economic conditions worsen or fail to improve, we may experience a material adverse impact on our business, operating results and financial condition.

A majority of our revenue comes from a small number of customers; if we lose any of our larger customers, our revenue could decline significantly.

Our three largest customers during the third quarter of 2003 were IBM, Ingenico and Square D (a division of Schneider Electric), which represented approximately 26.9%, 19.8% and 10.6%, respectively, of our total revenue for that period. Our top ten largest customers (including IBM, Ingenico and Square D) collectively represented approximately 91.1% of our total revenue during the third quarter of 2003. During the second quarter of 2002, the Company informed Dell of its intention to terminate its supply agreement with Dell and to end production over the third quarter of 2002. The Company's decision was taken after a review of the Company's return on capital requirements indicated that the customer's programs were not generating sufficient returns and, at the same time, were utilizing a disproportionate amount of working capital. We expect to continue to depend upon a relatively small number of customers for a significant percentage of our revenue. In addition to having a limited number of customers, we manufacture a limited number of products for each of our customers. If we lose any of our largest customers or any product line manufactured for one of our largest customers, we could experience a significant reduction in our revenue. Also, the insolvency of one or more of our largest customers or the inability of one or more of our largest customers to pay for its orders could decrease revenue. As many of our costs and operating expenses are relatively fixed, a reduction in net revenue can decrease our profit margins and adversely affect our business, financial condition and results of operations.

Our industry is very competitive and we may not be successful if we fail to compete effectively.

The electronics manufacturing services (EMS) industry is highly competitive. We compete against numerous domestic and foreign EMS providers including Celestica Inc., Flextronics International Ltd., Jabil Circuit, Inc., Sanmina-SCI, Inc., Solectron Corporation, Benchmark and Plexus. In addition, we may in the future encounter competition from other large electronics manufacturers that are selling, or may begin to sell, electronics manufacturing services. Many of our competitors have international operations, and some may have substantially greater manufacturing, financial, research and development and marketing resources and lower cost structures than we do. We also face competition from the manufacturing operations of current and potential customers, which are continually evaluating the merits of manufacturing products internally versus the advantages of using external manufacturers.

We may experience variability in our operating results, which could negatively impact the price of our shares.

Our annual and quarterly results have fluctuated in the past. The reasons for these fluctuations may similarly affect us in the future. Prospective investors should not rely on results of operations in any past period to indicate what our results will be for any future period. Our operating results may fluctuate in the future as a result of many factors, including:

- variations in the timing and volume of customer orders relative to our manufacturing capacity;
- variations in the timing of shipments of products to customers;

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- introduction and market acceptance of our customers' new products;
- changes in demand for our customers' existing products;
- the accuracy of our customers' forecasts of future production requirements;
- effectiveness in managing our manufacturing processes and inventory levels;
- changes in competitive and economic conditions generally or in our customers' markets;
- changes in the cost or availability of components or skilled labor; and
- difficulty in acquiring and retaining customers and obtaining competitive credit terms from suppliers due to weakened financial results.

In addition, most of our customers typically do not commit to firm production schedules more than 30 to 90 days in advance. Accordingly, we cannot forecast the level of customer orders with certainty. This makes it difficult to schedule production and maximize utilization of our manufacturing capacity. In the past, we have been required to increase staffing, purchase materials and incur other expenses to meet the anticipated demand of our customers. Sometimes anticipated orders from certain customers have failed to materialize, and sometimes delivery schedules have been deferred as a result of changes in a customer's business needs. Any material delay, cancellation or reduction of orders from our largest customers could cause our revenue to decline significantly. In addition, as many of our costs and operating expenses are relatively fixed, a reduction in customer demand can decrease our gross margins and adversely affect our business, financial condition and results of operations. On other occasions, customers have required rapid and unexpected increases in production, which have placed burdens on our manufacturing capacity.

Any of these factors or a combination of these factors could have a material adverse effect on our business, financial condition and results of operations.

We are dependent upon the electronics industry, which produces technologically advanced products with short life cycles.

Substantially all of our customers are in the electronics industry, which is characterized by intense competition, short product life-cycles and significant fluctuations in product demand. In addition, the electronics industry is generally subject to rapid technological change and product obsolescence. If our customers are unable to create products that keep pace with the changing technological environment, their products could become obsolete and the demand for our services could significantly decline. Our success is largely dependent on the success achieved by our customers in developing and marketing their products. Furthermore, this industry is subject to economic cycles and has in the past experienced downturns. A continued recession or a downturn in the electronics industry would likely have a material adverse effect on our business, financial condition and results of operations.

Shortage or price fluctuation in component parts specified by our customers could delay product shipment and affect our profitability.

A substantial portion of our revenue is derived from "turnkey" manufacturing. In turnkey manufacturing, we provide both the materials and the manufacturing services. If we fail to manage our inventory effectively, we may bear the risk of fluctuations in materials costs, scrap and excess inventory, all of which can have a material adverse effect on our business, financial condition and results of operations. We are required to forecast our future inventory needs based upon the anticipated demands of our customers. Inaccuracies in making these forecasts or estimates could result in a shortage or an excess of materials. In addition, delays, cancellations or reductions of orders by our customers could result in an excess of materials. A shortage of materials could lengthen production schedules and increase costs. An excess of materials may increase the costs

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of maintaining inventory and may increase the risk of inventory obsolescence, both of which may increase expenses and decrease profit margins and operating income.

Many of the products we manufacture require one or more components that we order from sole-source suppliers. Supply shortages for a particular component can delay productions of all products using that component or cause cost increases in the services we provide. In addition, in the past, some of the materials we use, such as memory and logic devices, have been subject to industry-wide shortages. As a result, suppliers have been forced to allocate available quantities among their customers and we have not been able to obtain all of the materials desired. Our inability to obtain these needed materials could slow production or assembly, delay shipments to our customers, increase costs and reduce operating income. Also, we may bear the risk of periodic component price increases. Accordingly, some component price increases could increase costs and reduce operating income. Also we rely on a variety of common carriers for materials transportation, and we route materials through various world ports. A work stoppage, strike or shutdown of a major port or airport could result in manufacturing and shipping delays or expediting charges, which could have a material adverse effect on our business, financial condition and results of operations.

We have experienced significant growth and significant retrenchment in a short period of time.

Since 1995, we have completed seven acquisitions. Acquisitions may involve numerous risks, including difficulty in integrating operations, technologies, systems, and products and services of acquired companies; diversion of management's attention and disruption of operations; increased expenses and working capital requirements; entering markets in which we have limited or no prior experience and where competitors in such markets have stronger market positions; and the potential loss of key employees and customers of acquired companies. In addition, acquisitions may involve financial risks, such as the potential liabilities of the acquired businesses, the dilutive effect of the issuance of additional equity securities, the incurrence of additional debt, the financial impact of transaction expenses and the amortization of goodwill and other intangible assets involved in any transactions that are accounted for using the purchase method of accounting, and possible adverse tax and accounting effects.

In 2001 we implemented a restructuring plan that called for significant retrenchment. We closed our Denver and Haverhill facilities and resized operations in Mexico and Ireland in an effort to reduce our cost structure. In February, 2002 the main customer of our Cork, Ireland facility was placed into administration as part of a financial restructuring. As a result, on March 19, 2002, we announced that we were closing our Cork, Ireland facility and that we were taking steps to place the subsidiary that operates that facility in voluntary administration. During the third quarter of 2002, the Company took further steps to realign its cost structure and plant capacity. We have also closed our interconnect facility in Donegal, Ireland and our sites in Austin, Texas and Charlotte, North Carolina. Manufacturing ceased in Austin, Texas during the first quarter of 2003, and we ceased operations at Donegal, Ireland and Charlotte, North Carolina during the second quarter of 2003. The Company sold its Appleton, Wisconsin manufacturing operations while retaining its Appleton design and engineering capabilities during the third quarter of 2003.

Retrenchment has caused, and is expected to continue to cause, strain on our infrastructure, including our managerial, technical and other resources. We may experience inefficiencies as we integrate operations from closed facilities to currently operating facilities and may experience delays in meeting the needs of transferred customers. In addition, we are reducing the geographic dispersion of our operations, which may make it harder for us to compete and may cause us to lose customers. The loss of customers could have a material adverse effect on our business, financial condition and results of operations.

Our rapid growth and subsequent retrenchment has placed and will continue to place a significant strain on management, on our financial resources, and on our information, operating and financial systems. If we are unable to manage effectively, it may have a material adverse effect on our business, financial condition and results of operations.

If we are unable to respond to rapidly changing technology and process development, we may not be able to compete effectively.

The market for our products and services is characterized by rapidly changing technology and continuing process development. The future success of our business will depend in large part upon our ability to maintain and enhance our technological capabilities, to develop and market products and services that meet

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changing customer needs, and to successfully anticipate or respond to technological changes on a cost-effective and timely basis. In addition, the EMS industry could in the future encounter competition from new or revised technologies that render existing technology less competitive or obsolete or that reduce the demand for our services. There can be no assurance that we will effectively respond to the technological requirements of the changing market. To the extent we determine that new technologies and equipment are required to remain competitive, the development, acquisition and implementation of such technologies and equipment may require us to make significant capital investments. There can be no assurance that capital will be available for these purposes in the future or that investments in new technologies will result in commercially viable technological processes.

Our business will suffer if we are unable to attract and retain key personnel and skilled employees.

Our business depends on our ability to continue to recruit, train and retain skilled employees, particularly executive management, engineering and sales personnel. Recruiting personnel in our industry is highly competitive. In addition, our ability to successfully implement our business plan depends in part on our ability to retain key management and existing employees. There can be no assurance that we will be able to retain our executive officers and key personnel or attract qualified management in the future. In connection with our restructuring, we significantly reduced our workforce. If we receive a significant volume of new orders, we may have difficulty recruiting skilled workers back into our workforce to respond to such orders and accordingly may experience delays that could adversely effect our ability to meet customers' delivery schedules.

Risks particular to our international manufacturing operations could adversely affect our overall results.

Our international manufacturing operations are subject to inherent risks, including:

- fluctuations in the value of currencies and high levels of inflation;
- longer payment cycles and greater difficulty in collecting amounts receivable;
- unexpected changes in and the burdens and costs of compliance with a variety of foreign laws;
- political and economic instability;
- increases in duties and taxation;
- imposition of restrictions on currency conversion or the transfer of funds;
- trade restrictions; and
- dependence on key customers.

We are subject to a variety of environmental laws, which expose us to potential financial liability.

Our operations are regulated under a number of federal, state, provincial, local and foreign environmental and safety laws and regulations, which govern, among other things, the discharge of hazardous materials into the air and water as well as the handling, storage and disposal of such materials. Compliance with these environmental laws is a major consideration for us because we use metals and other hazardous materials in our manufacturing processes. We may be liable under environmental laws for the cost of cleaning up properties we own or operate if they are or become contaminated by the release of hazardous materials, regardless of whether we caused such release. In addition we, along with any other person who arranges for the disposal of our wastes, may be liable for costs associated with an investigation and remediation of sites at which we have arranged for the disposal of hazardous wastes, if such sites become contaminated, even if we fully comply with applicable environmental laws. In the event of a contamination or violation of environmental laws, we could be held liable for damages including fines, penalties and the costs of remedial actions and could also be subject to revocation of our discharge permits. Any such revocations could require us to cease or limit production at one or more of our facilities, thereby having a material adverse effect on our operations. Environmental laws could also become more stringent over time, imposing greater compliance costs and increasing risks and penalties associated

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with any violation, which could have a material adverse effect on our business, financial condition and results of operations.

Item 3: Quantitative and Qualitative Disclosure about Market Risk

Interest Rate Risk

Our senior credit facility bears interest at a floating rate. The weighted average interest rate on our senior credit facility for the quarter ended September 28, 2003 was 6.6%. Our debt of \$74.0 million bore interest at 5.3% on September 28, 2003 based on the U.S. base rate. If the U.S. base rate increased by 10% our interest rate would have risen to 5.7 % and our interest expense would have increased by approximately \$0.1 million for the third quarter of 2003.

Foreign Currency Exchange Risk

Most of our sales are denominated in U.S. dollars. Most of our purchases are denominated in U.S. dollars, with the exception of Canadian and Mexican payroll and other various expenses denominated in local currencies, As a result we have relatively little exposure to foreign currency exchange risk.

Item 4. Controls and Procedures

- (a) Evaluation of Disclosure Controls and Procedures. As of the end of the period covered by this quarterly report, the Company's Chief Executive Officer and Principal Financial Officer have conducted an evaluation of the Company's disclosure controls and procedures. Based on their evaluation, the Company's Chief Executive Officer and Principal Financial Officer have concluded that the Company's disclosure controls and procedures are effective to ensure that information required to be disclosed by the Company in reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the applicable Securities and Exchange Commission rules and forms.
- (b) Changes in Internal Controls and Procedures. There were no significant changes in the Company's internal controls or in other factors that could significantly affect these controls subsequent to the date of the most recent evaluation of these controls by the Company's Chief Executive Officer and Principal Financial Officer.

PART II OTHER INFORMATION

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS.

(c) The terms of the Company's credit agreement require that the Company issue warrants to its lenders if it does not meet certain EBITDA targets as of each fiscal quarter end on the dates falling 45 days after the end of each fiscal quarter in 2003 and the first two fiscal quarters of 2004. The Company did not meet the applicable EBITDA target for the second fiscal quarter of 2003. Accordingly, the Company issued warrants as of August 13, 2003, certificated in the form included in Exhibit 10.44 to the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2002 filed with the Securities and Exchange Commission on March 27, 2003, for an aggregate of 228,210 shares of its common stock to its lenders in consideration for their extension of and continued performance under the credit facility. The warrants are immediately exercisable, have an exercise price per share of \$0.61 and expire on August 13, 2008. The issuance of warrants was exempt from registration under the Securities Act of 1933, as amended, pursuant to Section 4(2). The recipients of the warrants included only accredited investors.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.

(a) List of Exhibits:

- 10.1 Separation Agreement dated as of July 23, 2003 by and between SMTC Corporation and Frank Burke.
- 31.1 Certification of John Caldwell pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated November 17, 2003.
- 31.2 Certification of Marwan Kubursi pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated November 17, 2003.
- 32.1 Certification of John Caldwell, pursuant to Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, dated November 17, 2003.
- 32.2 Certification of Marwan Kubursi, pursuant to Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, dated November 17, 2003.

(b) Reports on Form 8-K:

On August 13, 2003, the Company furnished a Current Report on Form 8-K regarding the issuance of a press release announcing the Company's financial results for the three months ended June 29, 2003.

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SIGNATURES

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

SMTC CORPORATION

By: /s/ JOHN CALDWELL

Name: John Caldwell
Title: President and CEO

By: /s/ MARWAN KUBURSI

Name: Marwan Kubursi
Title: Principal Financial Officer

Date: November 17, 2003

EXHIBIT INDEX

Exhibit Number	Document
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[Letterhead of SMTC Corporation]

July 23, 2003

Frank Burke
112 Strath Avenue
Toronto, Ontario M8X 1R5

Dear Mr. Burke:

As we have discussed, your employment with SMTC Manufacturing Corporation of Canada ("SMTC Canada") serving as Chief Financial Officer of SMTC Canada, SMTC Corporation ("Holdings") and each of SMTC Canada's and Holdings' subsidiaries (SMTC Canada, Holdings and their subsidiaries, collectively, the "Company"), will end on August 31, 2003, (the "August Separation Date") or in the event that the Board of Directors requests you stay to assist the Company with a probable transaction, on September 30, 2003 (the "September Separation Date," and the August Separation Date or the September Separation Date, as appropriate, the "Separation Date"). The purpose of this letter is to confirm the agreement between you and SMTC Canada concerning your employment through the Separation Date and severance arrangements and other matters related to the termination of your employment with SMTC Canada, as follows:

1. **Bonus.** In consideration of your acceptance of this Agreement and upon your execution of this Agreement, SMTC Canada will pay you a bonus of Cdn\$150,000. In addition, on or before the Separation Date, SMTC Canada will pay you a final bonus of Cdn\$34,000 for the months of July and August 2003 and an additional Cdn\$16,000 for the month of September, if you stay until September 30, 2003 (the "September Bonus").

2. **Final Salary and Vacation Pay.** You will receive pay for all work you perform for SMTC Canada through the Separation Date, and (to the extent you do not use them after the date hereof) pay, at your final base rate of pay of Cdn\$300,000 per annum, for 12½ vacation days you will have earned, but not used by the August Separation Date or 3½ vacation days you will have earned, but not used by the September Separation Date. At your request, you may take these vacation days prior to your Separation Date, within reason, which shall be deducted from the vacation payout stated herein.

3. **Severance Benefits.** In addition to the other payments set out herein, in consideration of your acceptance of this Agreement and subject to your meeting in full your obligations under this Agreement, SMTC Canada will pay you a lump sum severance payment of Cdn\$128,000 on or before the Separation Date.

4. Sale of the Company. In the event a Sale Transaction is consummated at any time prior to the August Separation Date, you shall be paid the full amounts due per items 1 through 3 above, excluding the September Bonus, as if you had remained employed through the August Separation Date, on the date of the closing of such Sale Transaction. In the event a Sale Transaction is consummated at any time after August 31, 2003 and prior to the September Separation Date and you did not depart on the August Separation Date, you shall be paid the full amounts due per items 1 through 3 above as if you had remained employed through the September Separation Date, on the date of the closing of such Sale Transaction. For purposes of this Agreement, "Sale Transaction" means any transaction or series of transactions involving (a) an acquisition, merger, consolidation, or other business combination pursuant to which all or substantially all of the business or assets of the Company are, directly or indirectly, combined with another SMTC Canada; (b) the acquisition, directly or indirectly, by a buyer or buyers (which term shall include a "group" of persons as defined in Section 13(d) of the Securities Exchange Act of 1934, as amended), of all or substantially all of the equity interests and options of the Company or (c) the formation of a joint venture or partnership with the Company or direct investment in the Company for the purpose of effecting a transfer of all or substantially all of the Company's business or assets to a third party.

5. Future Services. In the event that SMTC Canada requests your services as an independent consultant after the September Separation Date, subject to our mutual consent, it is understood that your full-time services to SMTC Canada would be engaged on a month-to-month basis at a monthly rate of Cdn\$25,000, subject to termination by SMTC Canada at any time.

6. Stock Options. As of the Separation Date, you will be vested in 100,000 options to purchase Holding's common stock with an exercise prices varying from \$3.50 to \$16.00 per share (the "Exercisable Options"). The Exercisable Options will remain exercisable for ninety (90) days following the Separation Date. Any Exercisable Options not exercised during that time period shall be forfeited and shall terminate. Except as otherwise expressly provided in this paragraph 7, your rights and obligations with respect to the Exercisable Options shall remain unchanged and shall be governed by the terms of the applicable stock option plan, stock option grants, any agreements or other documents applicable to the Exercisable Options, and any other restrictions or provisions generally applicable to options granted to Company employees. All stock options previously granted to you that have not vested as of the Separation Date are forfeited and will be cancelled as of the Separation Date.

7. Withholding. All payments made by SMTC Canada under this Agreement shall be reduced by any tax or other amounts required to be withheld by SMTC Canada under applicable law and all other deductions authorized by you.

8. Acknowledgement of Full Payment. You acknowledge and agree that the payments provided under paragraphs 1, 2 and 3 of this Agreement are in complete satisfaction of any and all compensation due to you from SMTC Canada or any member of the Company, whether for services provided to SMTC Canada, the Company or otherwise, through the

Separation Date and that, except as expressly provided under this Agreement, no further compensation is owed to you.

9. Confidentiality and Non-Disparagement. Except as may be required by law, you agree that you will not disclose this Agreement or any of its terms or provisions, directly or by implication, except to members of your immediate family and to your legal and tax advisors. You also agree that you will not disparage or criticize the Company, its business, its management or its products, and that you will not otherwise do or say anything that could disrupt the good morale of the Company's employees or harm its interests or reputation. The Company, as represented by its senior executives, hereby agrees that it will not disparage or criticize you, your performance, and/or your conduct in good faith on behalf of the Company, and in the event that the Company is contacted by a third party seeking a reference, the Company undertakes to provide a positive performance appraisal and satisfaction with your activities.

10. Return of Company Documents and Other Property. In signing this Agreement, you agree that you will return to SMTC Canada, no later than the Separation Date, any and all documents, materials and information (whether in hard copy, on electronic media or otherwise) related to the business of the Company or any of its Affiliates (whether present or otherwise) and all keys, access cards, credit cards, computer hardware and software, telephones and telephone-related equipment and all other property of the Company and its Affiliates in your possession or control. Further, you represent and warrant that you will not retain any copy of any Company documents, materials or information (whether in hardcopy, on electronic media or otherwise), beyond the Separation Date. Recognizing that your employment with SMTC Canada has ended, you agree that after the Separation Date, you will not attempt to access or use any computer or computer network or system of the Company or any of its Affiliates, including without limitation the electronic mail systems. Further, you acknowledge that you will disclose to SMTC Canada, no later than the Separation Date, all passwords necessary or desirable to enable the Company to access all information which you have password-protected on any of its computer equipment or on its computer network or system. For purposes of this Agreement, "Affiliates" are all persons and entities directly or indirectly controlling, controlled by or under common control with the Company, where control may be by management authority or equity interest.

11. Other Agreements. You and SMTC Canada agree that as of the Separation Date, the Offer of Employment Letter Agreement between you and SMTC Manufacturing Corporation of Canada dated July 26, 2001, as amended, will automatically terminate and be of no further force and effect, provided that all consideration, as called for hereby has been paid.

12. Confidential Information. You acknowledge that information obtained by you during your employment with SMTC Canada concerning the business or affairs of the Company or any of its Affiliates ("Confidential Information") is the property of the Company. You shall not at any time during or after the Separation Date, without the prior written consent of the Board of Directors of Holdings, disclose to any unauthorized person or use for your own account or for the account of any person other than the Company or its Affiliates any Confidential Information, except to the extent necessary to comply with applicable laws or to the extent that such

information becomes generally known to and available for use by the public other than as a result of (i) your acts or (ii) during your employment with SMTC Canada, your omissions to act.

13. Non-Competition; Non-Solicitation.

(a) **Non-Competition.** You acknowledge that you are and will be in possession of Confidential Information, that your services are of unique and great value to the Company, and that some restrictions on your activities during and after your employment are necessary to protect the goodwill, Confidential Information and other legitimate interests of the Company and its Affiliates. Accordingly, from the Separation Date through February 29, 2004 (the "Non-Compete Period"), you shall not, directly or indirectly, own, manage, control, participate in, consult with, render services to, or in any manner engage in, any enterprise primarily engaged in the contract manufacturing of printed circuit boards or other electronic manufacturing services within any geographical area in which the Company or its Affiliates do business on the date of termination of your employment. Such geographical area shall include but not be limited to North America (including Mexico). Nothing herein shall prohibit you from being a passive owner of not more than 5% of any publicly-traded class of capital stock of any entity engaged in a competing business.

(b) **Non-Solicitation of Employees, Suppliers and Customers.** During the Non-Compete Period, you shall not (i) interfere with the relationship between the Company or any of its Affiliates, and any of their employees, or induce or attempt to induce any employee of the Company or its Affiliates to terminate his or her employment, (ii) hire directly or through another entity any person who was an employee of the Company (other than a former employee of the Company who left his or her employment without any inducement by you), (iii) induce or attempt to induce any independent contractor providing services to the Company or any of its Affiliates to terminate or diminish its relationship with the Company or its Affiliates, (iv) induce or attempt to induce any customer, supplier, licensee or other business relation of the Company or its Affiliates to cease doing business with such entity, or (v) in any way interfere in any material respect with the relationship between any such customer, supplier, licensee or business relation and the Company or its Affiliates.

(c) **Scope of Restriction.** If, at the time of enforcement of this paragraph 13, a court shall hold that the duration, scope or area restrictions stated herein are unreasonable under circumstances then existing, you agree that the maximum duration, scope or area reasonable under such circumstances shall be substituted for the stated duration, scope or area.

(d) **Necessity of Restraints.** You acknowledge that the restraints imposed by this paragraph 13 are reasonable and necessary for the protection of the Company and its Affiliates, and that any such entity would be harmed by a breach by you of these provisions.

14. Employee Cooperation. You agree to cooperate, within reason, with the Company and its Affiliates hereafter with respect to all matters arising during or related to your employment, including, but not limited to, all matters in connection with any litigation or other proceeding which may have arisen or which may arise following the signing of this Agreement.

SMTC Canada will reimburse your out-of-pocket expenses and any lost wages incurred in complying with Company requests hereunder, provided such expenses are authorized by SMTC Canada or Holdings in advance.

15. Release of Claims.

(a) In exchange for the special severance pay and benefits provided you under this Agreement, to which you would not otherwise be entitled, on your own behalf and that of your heirs, executors, administrators, beneficiaries, personal representatives and assigns, you agree that this Agreement shall be in complete and final settlement of any and all causes of action, rights or claims that you have had in the past, now have, or might now have, including, but not limited to, any causes of action, rights or claims in any way related to, connected with or arising out of your employment or its termination or pursuant to the Employment Standards Act, 2000 (Ontario), the Human Rights Code (Ontario), the fair employment practices statutes of the state, states province or provinces in which you have provided services to the Company or any of its Affiliates or any other federal, state, provincial or local law, regulation or other requirement and you hereby release and forever discharge the Company and its Affiliates and all of their respective past and present directors, shareholders, investors, officers, employees, agents and representatives, their successors and assigns, and all others connected with any of them, both individually and in their official capacities, from any and all such causes of action, rights or claims.

(b) Furthermore, in exchange for you executing this Agreement, the Company hereby agrees, on its own behalf and on behalf of any successors or assigns, employees, officers, directors, shareholders, investors, agents and representatives, their successor and assigns, both individually and in their official capacities (the "Company Releasees"), that this Agreement shall be in complete and final settlement of any and all causes of action, rights or claims that the Company Releasees have had in the past, now have, or might have in the future against up, your heirs, executors, administrators, beneficiaries, personal representatives and assigns. The Company hereby expressly undertakes and agrees to maintain all errors and omissions insurance presently in place with respect to you for a period of at least two (2) years after the Separation Date.

(c) This Agreement, including the release of claims set forth in this paragraph 15, creates legally binding obligations and SMTC Canada encourages you to seek the advice of legal counsel before signing this Agreement. In signing this Agreement, you give SMTC Canada assurance that you have signed it voluntarily and with a full understanding of its terms; that you have had sufficient opportunity, before signing this Agreement, to consider its terms and to consult with legal counsel, if you wished to do so, or to consult with any other of those persons to whom reference in made in the first sentence of paragraph 9 above; and that, in signing this Agreement, you have not relied on any promises or representations, express or implied, that are not set forth expressly in this Agreement.

16. Miscellaneous.

(a) This Agreement constitutes the entire agreement between you and SMTC Canada and supersedes all prior and contemporaneous communications, agreements and understandings, whether written or oral, with respect to your employment, its termination and all related matters, excluding only your obligations with respect to the securities of Holdings, all of which shall remain in full force and effect in accordance with their terms.

(b) This Agreement may not be modified or amended, and no breach shall be deemed to be waived, unless agreed to in writing by you and the Special Committee of the Board of Directors of SMTC Canada or its expressly authorized designee. The captions and headings in this Agreement are for convenience only and in no way define or describe the scope or content of any provision of this Agreement.

(c) The obligation of SMTC Canada to make payments to you or on your behalf to your personal representative in the event of your death, under this Agreement is expressly conditioned upon your continued full performance of your obligations under this Agreement and under paragraph 13 hereof.

(d) SMTC Canada may assign this Agreement to any of its subsidiaries or Affiliates, to any successor of SMTC Canada or the Company by reorganization, merger, consolidation or liquidation or to any transferee of all or substantially all of the business or assets of the Company. You may not assign this Agreement, which is personal to you.

(e) This Agreement shall be interpreted and construed in accordance with, and governed by, the laws of the Province of Ontario, and the parties hereby attorn to the exclusive jurisdiction of the Courts of the said province in connection with any dispute respecting this Agreement.

If the terms of this Agreement are acceptable to you, please sign, date and return it to me within five (5) days of the date you receive it. The enclosed copy of this letter, which you should also sign and date, is for your records. My signature on behalf of the Company signifies the Company's acceptance of all terms herein.

Sincerely,

SMTC CORPORATION

By: /s/ W.T. Brock

Name: William T. Brock

Title: Chairman

Accepted and agreed:

Signature: /s/ Frank Burke

Date: July 23, 2003

**CERTIFICATION PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

(b) CERTIFICATIONS

I, John Caldwell, certify that:

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

Date: November 17, 2003

/s/ JOHN CALDWELL

John Caldwell
President and Chief Executive Officer

**CERTIFICATION PURSUANT TO
SECTION 302 OF THE SARBANES-OXLEY ACT OF 2002**

(c) CERTIFICATIONS

I, Marwan Kubursi, certify that:

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

Date: November 17, 2003

/s/ MARWAN KUBURSI

Marwan Kubursi
Principal Financial Officer

**CERTIFICATION PURSUANT TO
SECTION 1350, CHAPTER 63 OF TITLE 18, UNITED STATES CODE,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

Pursuant to Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned, as chief executive officer of SMTC Corporation (the "Company"), does hereby certify that to the undersigned's knowledge:

- 1) the Company's quarterly report on Form 10-Q for the quarter ended September 28, 2003 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- 2) the information contained in the Company's quarterly report on Form 10-Q for the quarter ended September 28, 2003 fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ JOHN CALDWELL

John Caldwell
President and Chief Executive Officer

Date: November 17, 2003

A signed original of this written statement required by Section 906 has been provided to SMTC Corporation and will be retained by SMTC Corporation and furnished to the Securities and Exchange Commission or its staff upon request.

**CERTIFICATION PURSUANT TO
SECTION 1350, CHAPTER 63 OF TITLE 18, UNITED STATES CODE,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

Pursuant to Section 1350, Chapter 63 of Title 18, United States Code, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, the undersigned, as chief financial officer of SMTC Corporation (the "Company"), does hereby certify that to the undersigned's knowledge:

- 1) the Company's quarterly report on Form 10-Q for the quarter ended September 28, 2003 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- 2) the information contained in the Company's quarterly report on Form 10-Q for the quarter ended September 28, 2003 fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ MARWAN KUBURSI

Marwan Kubursi
Principal Financial Officer

Date: November 17, 2003

A signed original of this written statement required by Section 906 has been provided to SMTC Corporation and will be retained by SMTC Corporation and furnished to the Securities and Exchange Commission or its staff upon request.