

**UNITED STATES
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 27, 2020

OR

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

FOR THE TRANSITION PERIOD FROM TO

COMMISSION FILE NUMBER 000-31051

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.)

7050 WOODBINE AVENUE
MARKHAM, ONTARIO, CANADA L3R 4G8
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES) (ZIP CODE)

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

Securities registered pursuant to Section 12(b) of the Act:

| Title of each class | Trading Symbol(s) | Name of each exchange on which registered |
|---------------------|-------------------|---|
| Common Stock | SMTX | Nasdaq Global Select Market |

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

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

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

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company Emerging growth company

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

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

As of November 5, 2020, SMTC Corporation had 28,214,800 shares of common stock, par value \$0.01 per share, outstanding.

SMTC CORPORATION

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Part I FINANCIAL INFORMATION

Item 1 Financial Statements

Interim Consolidated Balance Sheets:
(Expressed in thousands of U.S. dollars)
(Unaudited)

| | September 27, 2020 | December 29, 2019 |
|--|-----------------------|----------------------|
| Assets | | |
| Current assets: | | |
| Cash | \$ 169 | \$ 1,368 |
| Accounts receivable — net (note 3) | 73,406 | 69,919 |
| Unbilled contract assets (note 3) | 42,736 | 26,271 |
| Inventories (note 3) | 51,537 | 47,826 |
| Prepaid expenses and other assets | 6,564 | 7,044 |
| Derivative assets (note 9) | 720 | — |
| Income taxes receivable | 160 | — |
| Total current assets | 175,292 | 152,428 |
| Property, plant and equipment — net (note 3) | 23,397 | 25,310 |
| Operating lease right of use assets — net | 5,897 | 3,330 |
| Goodwill (note 3) | 18,165 | 18,165 |
| Intangible assets — net (note 3) | 10,029 | 12,747 |
| Deferred income taxes — net | 555 | 540 |
| Deferred financing costs — net | 742 | 859 |
| Total assets | <u>\$ 234,077</u> | <u>\$ 213,379</u> |
| Liabilities and Shareholders' Equity | | |
| Current liabilities: | | |
| Revolving credit facility (note 4) | \$ 34,356 | \$ 34,701 |
| Accounts payable | 77,979 | 74,126 |
| Accrued liabilities (note 3) | 23,125 | 11,164 |
| Warrant liability (note 4) | 1,745 | 1,730 |
| Restructuring liability (note 10) | 364 | 1,597 |
| Income taxes payable | 254 | 157 |
| Current portion of long-term debt (note 4) | 2,188 | 1,250 |
| Current portion of operating lease obligations | 1,452 | 1,128 |
| Current portion of finance lease obligations | 1,818 | 1,226 |
| Total current liabilities | 143,281 | 127,079 |
| Long-term debt (note 4) | 32,513 | 33,750 |
| Operating lease obligations | 5,042 | 2,615 |
| Finance lease obligations | 8,696 | 8,838 |
| Total liabilities | 189,532 | 172,282 |
| Shareholders' equity: | | |
| Capital stock (note 5) | 508 | 508 |
| Additional paid-in capital | 293,864 | 293,389 |
| Deficit | (249,827) | (252,800) |
| | 44,545 | 41,097 |
| Total liabilities and shareholders' equity | <u>\$ 234,077</u> | <u>\$ 213,379</u> |

Commitments (note 11)

See accompanying notes to interim consolidated financial statements.

Interim Consolidated Statements of Operations and Comprehensive Income (loss)
(Expressed in thousands of U.S. dollars, except number of shares and per share amounts)
(Unaudited)

| | Three months ended | | Nine months ended | |
|--|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 27, 2020 | September 29, 2019 | September 27, 2020 | September 29, 2019 |
| Revenue (note 3) | \$ 99,547 | \$ 88,682 | \$ 285,091 | \$ 282,267 |
| Cost of sales (note 9) | 88,445 | 79,776 | 253,664 | 255,740 |
| Gross profit | 11,102 | 8,906 | 31,427 | 26,527 |
| Selling, general and administrative expenses | 6,710 | 6,549 | 21,036 | 19,908 |
| Change in fair value of contingent consideration | — | — | — | (3,050) |
| Restructuring charges (notes 3 and 10) | 871 | 6,454 | 525 | 8,624 |
| Operating income | 3,521 | (4,097) | 9,866 | 1,045 |
| Fair value measurement loss (gain) on warrant liability (note 4) | 133 | (858) | 15 | (919) |
| Interest expense (note 3) | 1,941 | 2,679 | 6,021 | 8,349 |
| Net income(loss) before income taxes | 1,447 | (5,918) | 3,830 | (6,385) |
| Income tax expense (recovery) (note 6): | | | | |
| Current | 286 | (103) | 872 | 592 |
| Deferred | (82) | (81) | (15) | 14 |
| | 204 | (184) | 857 | 606 |
| Net income (loss) and comprehensive income (loss) | <u>1,243</u> | <u>(5,734)</u> | <u>2,973</u> | <u>(6,991)</u> |
| Net income (loss) per share: | | | | |
| Basic | \$ 0.04 | \$ (0.20) | \$ 0.11 | \$ (0.28) |
| Diluted | \$ 0.04 | \$ (0.20) | \$ 0.10 | \$ (0.28) |
| Weighted average number of shares outstanding (note 7): | | | | |
| Basic | 28,214,800 | 28,057,763 | 28,207,943 | 24,954,875 |
| Diluted | <u>29,636,319</u> | <u>28,057,763</u> | <u>29,629,462</u> | <u>24,954,875</u> |

See accompanying notes to interim consolidated financial statements.

Interim Consolidated Statements of Changes in Shareholders' Equity

(Expressed in thousands of U.S. dollars)

Three months ended September 27, 2020

(Unaudited)

| | Common Shares | Capital stock | Additional paid-in capital | Deficit | Total Shareholders' equity |
|-----------------------------|-------------------|------------------|----------------------------------|---------------------|----------------------------------|
| Balance, June 28, 2020 | 28,214,800 | \$ 508 | \$ 293,706 | \$ (251,070) | \$ 43,144 |
| Stock-based compensation | — | — | 158 | — | 158 |
| Net income | — | — | — | 1,243 | 1,243 |
| Balance, September 27, 2020 | <u>28,214,800</u> | <u>\$ 508</u> | <u>\$ 293,864</u> | <u>\$ (249,827)</u> | <u>\$ 44,545</u> |

Three months ended September 29, 2019

(Unaudited)

| | Common Shares | Capital stock | Additional paid-in capital | Deficit | Total Shareholders' equity |
|--|-------------------|------------------|----------------------------------|---------------------|----------------------------------|
| Balance, June 30, 2019 | 28,011,088 | \$ 506 | \$ 292,829 | \$ (248,062) | \$ 45,273 |
| RSU vested and stock options exercised | 87,386 | 1 | 45 | — | 46 |
| Treasury stock | 21,264 | — | (75) | — | (75) |
| Stock-based compensation | — | — | 353 | — | 353 |
| Net loss | — | — | — | (5,734) | (5,734) |
| Balance, September 29, 2019 | <u>28,119,738</u> | <u>\$ 507</u> | <u>\$ 293,152</u> | <u>\$ (253,796)</u> | <u>\$ 39,863</u> |

See accompanying notes to interim consolidated financial statements.

| Nine months ended September 27, 2020 | Common Shares | Capital stock | Additional paid-in capital | Deficit | Total Shareholders' equity |
|--|-------------------|------------------|----------------------------------|---------------------|----------------------------------|
| Balance, December 29, 2019 | 28,195,300 | \$ 508 | \$ 293,389 | \$ (252,800) | \$ 41,097 |
| RSU vested and stock options exercised | 19,500 | — | — | — | — |
| Stock-based compensation | — | — | 475 | — | 475 |
| Net income | — | — | — | 2,973 | 2,973 |
| Balance, September 27, 2020 | <u>28,214,800</u> | <u>\$ 508</u> | <u>\$ 293,864</u> | <u>\$ (249,827)</u> | <u>\$ 44,545</u> |

| Nine months ended September 29, 2019 | Common Shares | Capital stock | Additional paid-in capital | Deficit | Total Shareholders' equity |
|--|-------------------|------------------|----------------------------------|---------------------|----------------------------------|
| Balance, December 30, 2018 | 23,189,381 | \$ 458 | \$ 278,648 | \$ (246,805) | \$ 32,301 |
| RSU vested and stock options exercised | 267,063 | 3 | 43 | — | 46 |
| Treasury stock | 21,264 | — | (75) | — | (75) |
| Issuance of common shares from rights offering | 4,642,030 | 46 | 13,998 | — | 14,044 |
| Stock-based compensation | — | — | 538 | — | 538 |
| Net loss | — | — | — | (6,991) | (6,991) |
| Balance, September 29, 2019 | <u>28,119,738</u> | <u>\$ 507</u> | <u>\$ 293,152</u> | <u>\$ (253,796)</u> | <u>\$ 39,863</u> |

Interim Consolidated Statements of Cash Flows
(Expressed in thousands of U.S. dollars)
(Unaudited)

| | Nine months ended | |
|---|-----------------------|-----------------------|
| | September 27, 2020 | September 29, 2019 |
| Cash provided by (used in): | | |
| Operations: | | |
| Net income (loss) | \$ 2,973 | \$ (6,991) |
| Items not involving cash: | | |
| Depreciation of property, plant and equipment | 4,767 | 4,902 |
| Amortization of intangible assets | 2,718 | 5,532 |
| Unrealized foreign exchange gain on unsettled forward exchange contracts | (720) | — |
| Write down of property, plant and equipment | — | 261 |
| Deferred income taxes expense (recovery) | (15) | 14 |
| Amortization of deferred financing fees and debt insurance costs | 892 | 1,300 |
| Stock-based compensation | 475 | 538 |
| Change in fair value of warrant liability | 15 | (919) |
| Change in fair value of contingent consideration | — | (3,050) |
| Change in non-cash operating working capital: | | |
| Accounts receivable | (3,487) | 11,778 |
| Unbilled contract assets | (16,465) | (6,385) |
| Inventories | (3,711) | 3,668 |
| Prepaid expenses and other assets | 480 | (1,095) |
| Income taxes receivable/payable | (63) | (116) |
| Accounts payable | 3,678 | (9,845) |
| Accrued liabilities | 11,964 | (265) |
| Restructuring liability | (1,233) | 2,736 |
| Net change in operating lease right of use asset and liability | 184 | 414 |
| | <u>2,452</u> | <u>2,477</u> |
| Financing: | | |
| Repayments (borrowing) of revolving credit facility | (345) | 9,820 |
| Repayment of long-term debt | (937) | (22,625) |
| Deferred financing fees | (137) | (371) |
| Principal repayments of finance lease obligations | (997) | (1,199) |
| Proceeds from issuance of common stock through exercise of stock options | — | 45 |
| Proceeds from issuance of common stock through rights offerings | — | 14,044 |
| | <u>(2,416)</u> | <u>(286)</u> |
| Investing: | | |
| Purchase of property, plant and equipment | (1,235) | (3,191) |
| | <u>(1,235)</u> | <u>(3,191)</u> |
| Decrease in cash | (1,199) | (1,000) |
| Cash, beginning of period | 1,368 | 1,601 |
| Cash, end of the period | <u>\$ 169</u> | <u>\$ 601</u> |
| Supplemental Information | | |
| Cash interest paid | \$ 5,643 | \$ 6,856 |
| Increase in operating right of use assets | \$ 3,707 | \$ 5,559 |
| Property, plant and equipment acquired through capital lease | \$ 1,447 | \$ 126 |
| Property, plant and equipment acquired that was unpaid in cash and included in accounts payable and accrued liabilities | \$ 404 | \$ 418 |

See accompanying notes to interim consolidated financial statements.

Unaudited Notes to Interim Consolidated Financial Statements
(in thousands)

1. Business and Basis of Presentation

Background

SMTC Corporation (the “Company,” “we,” “our,” or “SMTC”) is a provider of end-to-end electronics manufacturing services (“EMS”), including product design and engineering services, printed circuit board assembly (“PCBA”), production, enclosure, cable assembly, precision metal fabrication, systems integration and comprehensive testing services, configuration to order (“CTO”), build to order (“BTO”) and direct order fulfillment (“DOF”). SMTC has more than 50 manufacturing and assembly lines at strategically located facilities in the United States, Canada and Mexico that provide local support and manufacturing capabilities to our global customers. SMTC’s services extend over the entire electronic product life cycle from new product development and new product introduction (“NPI”) through to growth, maturity and end of life phases.

Basis of Presentation

The accompanying unaudited interim consolidated financial statements of the Company have been prepared in accordance with the accounting principles and methods of application disclosed in the audited consolidated financial statements within the Company’s Form 10-K for the fiscal period ended December 29, 2019, (“Form 10-K”) filed with the Securities and Exchange Commission (the “SEC”) on March 13, 2020. The accompanying unaudited interim consolidated financial statements include adjustments of a normal, recurring nature that are, in the opinion of management, necessary for a fair statement of the consolidated financial statements under generally accepted accounting principles in the United States (“U.S. GAAP”). These unaudited interim consolidated financial statements should be read in conjunction with the Company’s audited consolidated financial statements contained in the Company’s Form 10-K. The consolidated balance sheet at December 29, 2019 was derived from the audited annual consolidated financial statements, but does not contain all of the footnote disclosures from the annual consolidated financial statements.

The preparation of financial statements requires management to make estimates and assumptions that affect the amounts reported in the unaudited condensed consolidated financial statements and accompanying notes. Due to the COVID-19 pandemic, the global economy and financial markets have been disrupted and there continues to be significant uncertainty about the length and severity of the consequences caused by the pandemic. Consequently, actual results could differ materially from these estimates and be significantly affected by the severity and duration of the pandemic, the extent of actions to contain or treat COVID-19, how quickly and to what extent normal economic and operating activity can resume, and the severity and duration of the global economic downturn that results from the pandemic.

Unless otherwise specified or the context requires otherwise, all statements in these notes to the interim consolidated financial statements regarding financial figures are expressed in thousands of U.S. dollars.

As at September 27, 2020, the additional funds available to borrow under our PNC Facility (as described and defined in note 4 below) after deducting the current borrowing base conditions and subject to debt covenants, should the Company require additional funding during the COVID-19 pandemic, was \$30,464 (December 29, 2020 - \$21,644).

Transition of China Manufacturing

During the fourth quarter of 2019, we ceased manufacturing in China and began to relocate the equipment used at our Dongguan manufacturing facility to our other North American sites. During the first quarter of 2020, we completed final shipments for customers serviced at our Chinese manufacturing facility and the relocation of that equipment. Customer concerns about uncertainties relating to the prolonged impact of tariffs and macro-economic factors caused a number of our customers to begin to re-evaluate demand for some of their products and reconsider where they outsource their manufacturing. These factors ultimately resulted in the decision to close the manufacturing facility. The closure of the Dongguan facility was substantially completed as at September 27, 2020 with final deregistration steps expected to be completed during the fourth quarter of 2020.

2. Accounting Pronouncements

Recent Accounting Pronouncements Adopted

In August 2018, the FASB published ASU 2018-13: Fair Value Measurement (Topic 820): Disclosure Framework – Changes to the Disclosure Requirements for Fair Value Measurement. The amendment includes the removal, modification and addition of disclosure requirements under Topic 820. The amendments in this ASU are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2019. The impact of the adoption of the standard expands the disclosure of certain assets and liabilities recorded at fair value.

In March 2020, the FASB published ASU 2020-04: Reference Rate Reform (Topic 848): Facilitation of the Effects of Reference Rate Reform on Financial Reporting. The amendments in this update are elective and provide optional guidance for a limited period of

time to ease the potential burden in accounting for (or recognizing the effects of) reference rate reform on financial reporting. The amendments in this Update are effective for all entities as of March 12, 2020, through December 31, 2022. An entity may elect to apply the amendments for contract modifications by Topic or Industry Subtopic as of any date from the beginning of an interim period that includes or is subsequent to March 12, 2020, or prospectively from a date within an interim period that includes or is subsequent to March 12, 2020, up to the date that the financial statements are available to be issued. Once elected for a Topic or an Industry Subtopic, the amendments in this Update must be applied prospectively for all eligible contract modifications for that Topic or Industry Subtopic. The impact of the adoption of the standard is not material to the Company, as alternative reference rates are available under the agreements governing the financial instruments.

Recent Accounting Pronouncements Not Yet Adopted

In May 2016, the FASB published ASU 2016-13: Financial Instruments – Credit losses (Topic 326): Measurement of Credit Losses on Financial Instruments. The main objective of Topic 326 is to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments and other commitments to extend credit held by a reporting entity at each reporting date. To achieve this objective, the amendments in this update replace the incurred loss impairment methodology in current U.S. GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. In April 2019, the FASB published ASU 2019-04 Codification Improvements to Topic 326, Financial Instruments – Credit Losses, which made certain amendments and corrections to the original codification. In May 2019, the FASB published ASU 2019-05 Financial Instruments – Credit losses (Topic 326) which made transitional relief available, specifically allowing the option to elect a fair value option for financial instruments measured at amortized cost. In November 2019, the FASB published ASU 2019-11 Codification Improvements to Topic 326, Financial Instruments – Credit losses, which made certain amendments and corrections to the original codification. In November 2019, the FASB published ASU 2019-10 Financial Instruments – Credit losses (Topic 326), which made certain amendments to the effective dates of the new standard. The amendment is effective for the Company for years beginning after December 15, 2022 including interim periods with those years. On March 9, 2020, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2020-03 Codification Improvements to Financial Instruments. The Company is currently evaluating the impact of this accounting standard, but it is expected that the new standard may result in additional credit losses being recorded.

In January 2017, the FASB published ASU 2017-04: Intangibles – Goodwill and Other (Topic 350): Topic 350 seeks to simplify goodwill impairment testing requirements for public entities. Under the amendments in this update, an entity should perform its annual, or interim, goodwill impairment test by comparing the fair value of a reporting unit with its carrying amount. An entity should recognize an impairment charge for the amount by which the carrying amount exceeds the reporting unit's fair value; however, the loss recognized should not exceed the total amount of goodwill allocated to that reporting unit. Additionally, an entity should consider income tax effects from any tax-deductible goodwill on the carrying amount of the reporting unit when measuring the goodwill impairment loss, if applicable. The FASB also eliminated the requirements for any reporting unit with a zero or negative carrying amount to perform a qualitative assessment and, if it fails that qualitative test, to perform Step 2 of the goodwill impairment test. Therefore, the same impairment assessment applies to all reporting units. An entity is required to disclose the amount of goodwill allocated to each reporting unit with a zero or negative carrying amount of net assets. The amendments in this ASU are effective for all entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2022. The Company is currently evaluating the impact of this accounting standard. However, it is expected that this may reduce the complexity of evaluating goodwill for impairment.

In December 2019, the FASB published ASU 2019-12: Income Taxes (Topic 740): Simplifying the Accounting for income taxes. The purpose of this codification is to simplify the accounting for income taxes, which addresses a number of topics including but not limited to the removal of certain exceptions currently included in the standard related to intraperiod allocation when there are losses, in addition to calculation of income taxes when current year-to-date losses exceed anticipated loss for the year. The amendment also simplifies accounting for certain franchise taxes and disclosure of the effect of enacted change in tax laws or rates. Topic 740 is effective for public entities for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2020. The impact of the adoption of the standard has not yet been determined and is being evaluated.

3. Interim Consolidated financial statement details

The following consolidated financial statement details are presented as of the period ended for the consolidated balance sheets and for the periods ended for each of the consolidated statements of operations and comprehensive income (loss).

Consolidated Balance Sheets

Accounts receivable – net:

| | <u>September 27, 2020</u> | <u>December 29, 2019</u> |
|---------------------------------|-------------------------------|------------------------------|
| Trade accounts receivable | \$ 75,000 | \$ 71,113 |
| Other receivables | 731 | 1,098 |
| Allowance for doubtful accounts | (2,325) | (2,292) |
| Total | <u>\$ 73,406</u> | <u>\$ 69,919</u> |

The allowance for doubtful accounts pertains primarily to one customer previously serviced out of Dongguan China. This was provisioned and included with the restructuring charges for the closure of the facility in 2019. Refer to note 10 for further details of the restructuring. To date, there has been no material impact of the COVID-19 pandemic on the allowance for doubtful accounts.

Unbilled contract assets

| | <u>September 27, 2020</u> | <u>December 29, 2019</u> |
|---------------------------|-------------------------------|------------------------------|
| Opening | \$ 26,271 | \$ 20,405 |
| Contract assets additions | 276,330 | 350,709 |
| Contract assets invoiced | (259,865) | (344,843) |
| Ending | <u>\$ 42,736</u> | <u>\$ 26,271</u> |

Inventories:

| | <u>September 27, 2020</u> | <u>December 29, 2019</u> |
|----------------------------|-------------------------------|------------------------------|
| Raw materials | \$ 51,783 | \$ 48,067 |
| Parts and other | 292 | 586 |
| Provision for obsolescence | (538) | (827) |
| Total | <u>\$ 51,537</u> | <u>\$ 47,826</u> |

The provision for obsolescence primarily pertains to customers previously serviced out of the Dongguan facility. These have been provisioned and included with the restructuring charges for the closure of the facility in 2019. Refer to note 10 for further details of the restructuring.

Property, plant and equipment – net:

| | September 27, 2020 | December 29, 2019 |
|--|-----------------------|----------------------|
| Cost: | | |
| Land | \$ 1,648 | \$ 1,648 |
| Buildings (b) | 18,985 | 18,985 |
| Machinery and equipment (a) (e) | 44,116 | 42,732 |
| Office furniture and equipment (c) (e) | 869 | 1,005 |
| Computer hardware and software (d) (e) | 3,940 | 3,979 |
| Leasehold improvements (e) | 4,447 | 4,265 |
| | <u>74,005</u> | <u>72,614</u> |
| Less accumulated depreciation: | | |
| Land | — | — |
| Buildings (b) | (11,220) | (10,392) |
| Machinery and equipment (a) (e) | (33,727) | (31,192) |
| Office furniture and equipment (c) (e) | (423) | (546) |
| Computer hardware and software (d) (e) | (3,162) | (3,289) |
| Leasehold improvements (e) | (2,076) | (1,885) |
| | <u>(50,608)</u> | <u>(47,304)</u> |
| Property, plant and equipment—net | <u>\$ 23,397</u> | <u>\$ 25,310</u> |

- (a) Included within machinery and equipment were assets under finance leases with costs of \$4,193 and \$2,275 and associated accumulated depreciation of \$1,539 and \$974 as of September 27, 2020 and December 29, 2019, respectively. The related depreciation expense for the three months ended September 27, 2020 and September 29, 2019 was \$134 and \$142, respectively. The related depreciation expense for the nine months ended September 27, 2020 and September 29, 2019 was \$56 and \$426, respectively.
- (b) Included within buildings are costs associated with Melbourne facility under finance leases of \$9,082 and associated accumulated depreciation of \$1,504 and \$900 as of September 27, 2020 and December 29, 2019, respectively. The related depreciation expense for the three months ended September 27, 2020 and September 29, 2019 was \$201 and \$201, respectively. The related depreciation expense for nine months ended September 27, 2020 and September 29, 2019 was \$604 and \$603, respectively.
- (c) Included within office furniture and equipment were assets under finance leases with costs of \$307 and \$307 and associated accumulated depreciation of \$101 and \$52 as of September 27, 2020 and December 29, 2019, respectively. The related depreciation expense for the three months ended September 27, 2020 and September 29, 2019 was \$16 and \$9, respectively. The related depreciation expense for the nine months ended September 27, 2020 and September 29, 2019 was \$49 and \$29, respectively.
- (d) Included within computer hardware and software were assets under finance leases with costs of \$91 and associated accumulated depreciation of \$73 and \$51 as of September 27, 2020 and December 29, 2019, respectively. The related depreciation expense for the three months ended September 27, 2020 and September 29, 2019 was \$7 and \$8, respectively. The related depreciation expense for the nine months ended September 27, 2020 and September 29, 2019 was \$22 and \$23, respectively.
- (e) Fully depreciated property, plant and equipment with cost of \$1,466 and accumulated amortization of \$1,463 was written off in the nine months ended September 27, 2020.

Intangible assets:

| | September 27, 2020 | December 29, 2019 |
|--------------------------------|-----------------------|----------------------|
| Cost: | | |
| Customer relationships | \$ 12,350 | \$ 12,350 |
| Order backlog | 6,990 | 6,990 |
| Trade name | 1,300 | 1,300 |
| Non-compete agreements | 360 | 360 |
| | <u>21,000</u> | <u>21,000</u> |
| Less accumulated amortization: | | |
| Customer relationships | (2,340) | (1,414) |
| Order backlog | (6,990) | (5,333) |
| Trade name | (1,300) | (1,300) |
| Non-compete agreements | (341) | (206) |
| | <u>(10,971)</u> | <u>(8,253)</u> |
| Intangible assets—net | <u>\$ 10,029</u> | <u>\$ 12,747</u> |

These intangible assets arose from the acquisition of MC Assembly Holdings Inc. (“MC Assembly”) in November 2018 and were allocated to the following operating segments:

| | September 27, 2020 | December 29, 2019 |
|--------|-----------------------|----------------------|
| U.S. | \$ 3,009 | \$ 3,824 |
| Mexico | 7,020 | 8,923 |
| Total | <u>\$ 10,029</u> | <u>\$ 12,747</u> |

Amortization expense of \$2,718 was recorded in cost of sales in the consolidated statement of operations and comprehensive income(loss) for the nine months ended September 27, 2020, and \$5,532 for the nine months ended September 29, 2019. Amortization expense for the next five years and thereafter is as follows:

| | |
|---------------------|------------------|
| 2020 | \$ 328 |
| 2021 | 1,235 |
| 2022 | 1,235 |
| 2023 | 1,235 |
| 2024 | 1,235 |
| 2025 and thereafter | 4,761 |
| Total amortization | <u>\$ 10,029</u> |

Goodwill:

The carrying value of goodwill as at September 27, 2020 was \$18,165 (December 29, 2019 – \$18,165). This goodwill arose from the acquisition of MC Assembly in November 2018 and was allocated to the following operating segments that are expected to benefit from the synergies of this business combination and has not changed since the acquisition:

| | September 27, 2020 | December 29, 2019 |
|--------|-----------------------|----------------------|
| U.S. | \$ 5,449 | \$ 5,449 |
| Mexico | 12,716 | 12,716 |
| Total | <u>\$ 18,165</u> | <u>\$ 18,165</u> |

The carrying value of goodwill is assessed annually at year-end and at each reporting period for impairment triggers to determine whether there exists any indicators of impairment. The assessment is done at the operating segment level as the group of components (production facilities) within each operating segment all have similar economic characteristics. Our business operations have generally performed as expected during the first nine months of 2020. While the COVID-19 pandemic creates significant uncertainty, in the near term, the Company did not identify any triggering events as at September 27, 2020.

Accrued liabilities:

| | September 27, 2020 | December 29, 2019 |
|-----------------------|-----------------------|----------------------|
| Payroll | \$ 7,515 | \$ 5,504 |
| Customer related | 6,347 | 2,185 |
| Deferred revenue | 5,915 | — |
| Vendor related | 1,436 | 1,742 |
| Professional services | 644 | 612 |
| Interest | 330 | 860 |
| Other | 938 | 261 |
| Total | <u>\$ 23,125</u> | <u>\$ 11,164</u> |

Deferred Revenue is recorded when the Company invoices and becomes eligible to receive payment for goods or services prior to the transferring of goods or services to the customer under the terms of the contract (i.e., all revenue recognition criteria are not yet met), which is included within accrued liabilities. As of September 27, 2020 and December 29, 2019, the balance of deferred revenue was \$5,915 and Nil, respectively. Revenue of \$899 was recognized during the nine months ended September 27, 2020. The accounts receivable balances associated with the deferred revenue invoicing was \$5,915 as at September 27, 2020 with no corresponding deferred revenue invoices in accounts receivable as at December 29, 2019. Deferred revenue is recognized into revenue when all revenue recognition criteria are met.

Consolidated Statements of Operations and Comprehensive Income (Loss)

Interest expense:

| | Three months ended | | Nine months ended | |
|---|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 27, 2020 | September 29, 2019 | September 27, 2020 | September 29, 2019 |
| Long-term debt | \$ 1,012 | \$ 1,135 | \$ 3,080 | \$ 4,596 |
| Revolving credit facility | 415 | 597 | 1,449 | 1,813 |
| Amortization of deferred financing fees | 59 | 50 | 169 | 122 |
| Amortization of debt issuance costs | 245 | 705 | 723 | 1,178 |
| Obligations under finance leases | 195 | 192 | 575 | 640 |
| Other interest | 15 | — | 25 | — |
| Total | <u>\$ 1,941</u> | <u>\$ 2,679</u> | <u>\$ 6,021</u> | <u>\$ 8,349</u> |

4. Debt

(a) Revolving credit and long-term debt facilities

| | September 27, 2020 | December 29, 2019 |
|-----------------------------------|-----------------------|----------------------|
| Revolving credit facility | <u>\$ 34,356</u> | <u>\$ 34,701</u> |
| Term loans: | | |
| Term loan A facility | \$ 37,813 | \$ 38,750 |
| Less deferred debt issue costs | (1,928) | (2,286) |
| Less unamortized discount on debt | (1,184) | (1,464) |
| Total term loans | \$ 34,701 | \$ 35,000 |
| Less current portion | (2,188) | (1,250) |
| Long term portion | <u>\$ 32,513</u> | <u>\$ 33,750</u> |

The Company borrows money under an Amended and Restated Revolving Credit and Security Agreement with PNC Bank, National Association (“PNC”) which governs the Company’s revolving credit facility (“PNC Facility”). The PNC Facility has a term ending on November 8, 2023. Advances made under the PNC Facility bear interest at the U.S. base rate plus a grid ranging from 0.50% to 1.00% or 1, 2 or 3-month fully-absorbed PNC LIBOR plus a grid ranging from 1.50% to 2.00%. The base commercial lending rate should approximate U.S. prime rate.

The Company also borrows money under a Financing Agreement (the “Financing Agreement”), by and among the Company and certain of its subsidiaries, the lenders party to the Financing Agreement from time to time (collectively, the “Lenders”), and TCW Asset Management Company, LLC, as collateral agent for the Lenders (“TCW”). The Financing Agreement governs a term loan A facility (the “Term A Loan Facility” and together with the PNC Facility, the “Credit Facilities” and previously governed a term loan B facility (the “Term Loan B Facility”) until it was paid in full on July 3, 2019. The Term Loan A Facility matures on November 8, 2023 (the “Maturity Date”). The Term Loan A Facility bears interest LIBOR plus an applicable margin of 8.75% through June 30, 2020, and borrowings under the Financing Agreement will thereafter bear interest at LIBOR plus an applicable margin ranging from 7.25% to 8.75%. Payments made under the Term Loan A Facility at any time prior to the Maturity Date (other than scheduled amortization payments and mandatory prepayments) are subject to an applicable premium equal to the amount of such payment multiplied by (i) 3.00% in the event that such payment occurs before November 8, 2019, (ii) 2.00% in the event that such payment occurs after November 8, 2019 and on or before November 8, 2020, and (iii) 1.00% in the event that such payment occurs after November 8, 2020 and on or before November 8, 2021. No such applicable premium is payable for any payment of loans made under the Term Loan A Facility occurring after November 8, 2021.

On June 26, 2020, the Company, entered into the Fourth Amendment to the Amended and Restated Revolving Credit and Security Agreement (“PNC Fourth Amendment”) and the Fifth Amendment to the Financing Agreement (“TCW Fifth Amendment”). The PNC Fourth Amendment and TCW Fifth Amendment, among other things, amend the definition of “Consolidated EBITDA” by permitting an addback for (i) non-recurring labor costs, temporary employee bonuses to reduce absenteeism, personal protective equipment costs, facility sanitation costs, and excess freight and logistics costs, not to exceed \$1,200, and (ii) restructuring and severance charges, accruals and reserves in connection with permanent headcount reductions, in an aggregate amount not to exceed \$1,000 with respect to corporate selling, general and administrative employees, in each case, for the period from June 1, 2020, to and including July 31, 2020. The PNC Fourth Amendment and TCW Fifth Amendment also amends the definition of “Permitted Purchase Money Indebtedness” to (i) allow for Indebtedness (as defined in the PNC Agreement) pursuant to financing provided by a third party lender for any fixed or tangible assets acquired prior to the June 26, 2020, and (ii) increase the aggregate principal amount of all Indebtedness (as defined in the PNC Agreement and Financing Agreement) permitted under the PNC Agreement to \$3,750.

On September 25, 2020, the Company, entered into the Fifth Amendment to the Amended and Restated Revolving Credit and Security Agreement (“PNC Fifth Amendment”). The PNC Fifth Amendment, among other things, (i) amends the definition of “Consolidated EBITDA” by permitting an addback for non-recurring labor costs, temporary employee bonuses to reduce absenteeism, personal protective equipment costs, facility sanitation costs, and excess freight and logistics costs, not to exceed an additional \$1,500 for the three months ended September 27, 2020, and (ii) provides for borrowings of up to \$2,000 on certain consigned assets. On September 25, 2020, the Company entered into the Sixth Amendment to the Financing Agreement (“TCW Sixth Amendment”). The TCW Sixth Amendment, among other things, amends the definition of “Consolidated EBITDA” by permitting an addback for non-recurring labor costs, temporary employee bonuses to reduce absenteeism, personal protective equipment costs, facility sanitation costs and excess freight and logistics costs, not to exceed an additional \$1,500 for the three months ended September 27, 2020.

As at September 27, 2020, the additional funds available to borrow under the PNC Facility after deducting the current borrowing base conditions were \$0,464 (December 29, 2019 - \$21,644). The maximum amount of funds that could be available under the PNC Facility is \$65,000. However, availability under the PNC Facility is subject to certain conditions, including borrowing base conditions based on eligible inventory and accounts receivable, and certain conditions as determined by PNC. The Company is required to use a “lock-box” arrangement for the PNC Facility, whereby remittances from customers are swept daily to reduce the borrowings under this facility.

At September 27, 2020, \$34,356 (December 29, 2019 - \$34,701) was outstanding under the PNC Facility and is classified as a current liability based on the requirement to hold a “lock-box” under the terms of the PNC Facility.

At September 27, 2020, \$37,813 (December 29, 2019 - \$38,750) was outstanding under the TCW Term Loan A Facility. The TCW Facilities are reported on the consolidated balance sheet net of deferred financing fees of \$1,928 (December 29, 2019 - \$2,286) and a discount on debt of \$1,184 (December 29, 2019 - \$1,464) related to the outstanding warrants described below.

The Credit Facilities are joint and several obligations of the Company and its subsidiaries that are borrowers under the Credit Facilities and are jointly and severally guaranteed by other subsidiaries of the Company. Repayment under the PNC Facility and Term A Loan Facility are collateralized by the assets of the Company and each of its subsidiaries.

(b) Covenants

The Credit Facilities contain certain financial and non-financial covenants, including restrictions on dividend payments. The financial covenants require the Company to maintain a fixed charge coverage ratio and a total leverage ratio quarterly during the term of the Credit Facilities.

The Company was in compliance with the covenants included in the Credit Facilities as at September 27, 2020. The Company's continued financial covenant compliance will depend on key variables, including the Company's cash flow from earnings before interest, income taxes and depreciation as well as debt levels. For context, assuming no change to forecast debt balances, a reduction of approximately 14% of forecast earnings before interest, income taxes, depreciation and amortization as defined in PNC Agreement and Financing Agreement over the next twelve month period, could jeopardize covenant compliance at the end of our third quarter 2021. The Company attempts to address risks of covenant compliance by taking measures to reduce its inventory, revolving credit facility and term debt balances as necessary.

Market conditions, including the implications of the COVID-19 pandemic, may negatively impact our ability to secure and source alternative methods of financing. We do not currently foresee a material impact in the short term based on our working capital needs, however if a number of our customers reduce or temporarily cease payments to us, this would present a risk and negatively impact our cash flow and ability to meet our working capital obligations to operate our business, which could require us to secure alternative methods of financing.

The Company continues to monitor operations and results closely and manage debt levels relative to our operational results to ensure compliance with its lenders covenants.

(c) Warrant liability

On November 8, 2018, 504,735 warrants were issued to TCW in connection with the Financing Agreement and are outstanding as at September 27, 2020. As a result of the anti-dilution provisions contained in the warrants that were triggered in connection with the Rights Offering and the Registered Direct Offering in June 2019, the warrants were exercisable to purchase an additional 7,214 shares of common stock (or a total of 511,949 shares) at September 27, 2020. These warrants are exercisable on a cashless basis, or for an exercise price of \$0.01. The Company initially recorded the value of the warrants as a warrant liability with a corresponding discount on the long-term debt in the amount of \$1,898. The fair value has been assessed at \$3.41 per unit or \$1,746 as at September 27, 2020 (\$3.38 per unit or \$1,730 – December 29, 2019). The fair value of the warrant obligation is presented as a warrant liability on the consolidated balance sheet with changes to the fair value recorded each reporting period as either a gain or a loss in the consolidated statement of operations and comprehensive income (loss).

5. Capital stock

Common shares

Issued and outstanding:

The issued and outstanding number of common shares included in shareholders' equity consisted of the following:

| | Number of shares | \$ |
|--|----------------------|---------------|
| Balance at December 29, 2019 | \$ 28,195,300 | \$ 508 |
| New share issuance-vested stock awards | 19,500 | - |
| Balance September 27, 2020 | <u>\$ 28,214,800</u> | <u>\$ 508</u> |

Stock Options

For more detailed information regarding the Company's stock option arrangements, see Note 7 of the consolidated financial statements within the Company's Form 10-K for the fiscal period ended December 29, 2019. During the nine months ended September 27, 2020, there were no stock options granted, exercised or forfeited. A summary of stock option activity for the nine months ended September 27, 2020 is as follows:

| | Number of options | Weighted average exercise price | Aggregate intrinsic value | Weighted average remaining contractual term (years) |
|-----------------------------------|-------------------|---------------------------------|---------------------------|---|
| Outstanding at December 29, 2019 | 2,344,374 | \$ 2.14 | 2,016 | 7.9 |
| Options granted | — | — | — | — |
| Options exercised | — | — | — | — |
| Options forfeited | — | — | — | — |
| Outstanding at September 27, 2020 | 2,344,374 | 2.14 | 2,049 | 7.2 |
| Exercisable at September 27, 2020 | 1,088,140 | 1.55 | 2,024 | 6.5 |

During the three-month periods ended September 27, 2020 and September 29, 2019, the Company recorded stock-based compensation expense related to stock options and a corresponding increase in additional paid-in capital of \$57 and \$57, respectively. During the nine months ended September 27, 2020 and September 29, 2019, the Company recorded stock-based compensation expense related to stock options and a corresponding increase in additional paid-in capital of \$172 and \$120, respectively.

Certain stock options outstanding have market conditions such that the awards are vested and exercisable only if the Company's stock exceeds specified targets during the vesting period. If the market conditions are not met, the stock options will not vest and will expire.

Restricted Stock Units and Restricted Stock Awards

For more detailed information regarding the Company's Restricted Stock Units ("RSU") and Restricted Stock Awards ("RSA") arrangements, see Note 7 of the consolidated financial statements within the Company's Form 10-K for the fiscal period ended December 29, 2019. During the nine months ended September 27, 2020, 178,000 RSUs were granted. A summary of the RSU activity for the nine months ended September 27, 2020 is as follows:

| | Outstanding RSU | Weighted average stock price | Weighted average remaining contractual term (years) |
|--|-----------------|------------------------------|---|
| Outstanding balance at December 29, 2019 | 348,000 | \$ 3.16 | 2.23 |
| RSU granted | 178,000 | 2.92 | |
| RSU vested and issued in common shares | (19,500) | 1.28 | |
| RSU forfeited | (27,500) | (1.28) | |
| Outstanding at September 27, 2020 | 479,000 | 3.14 | 2.18 |

Stock based compensation recognized during the three-month period ended September 27, 2020 and September 29, 2019 related to the restricted stock units was \$01 and \$296, respectively. Stock based compensation recognized during the nine months ended September 27, 2020, and September 29, 2019, related to the restricted stock units was \$303 and \$418, respectively.

6. Income taxes

During the nine months ended September 27, 2020 and September 29, 2019, the Company recorded current income tax expense \$72 and \$592, respectively, in connection with U.S. state taxes and taxes on profits in certain foreign jurisdictions, and deferred income tax (recovery) expense of (\$15) and \$14, respectively, in connection with temporary differences related to the Mexican operations.

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. Guidance under ASC 740, Income Taxes (“ASC 740”) 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. The U.S., Canadian and Asian jurisdictions continue to have a full valuation allowance recorded against the deferred tax assets.

7. Earnings per common share

The following table details the weighted average number of common shares outstanding for the purposes of computing basic and diluted earnings per common share for the following periods:

| <i>(Number of common shares)</i> | Three months ended | | Nine months ended | |
|---|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 27, 2020 | September 29, 2019 | September 27, 2020 | September 29, 2019 |
| Basic weighted average shares outstanding | 28,214,800 | 28,057,763 | 28,207,943 | 24,954,875 |
| Dilutive stock awards (a,b) | 1,421,519 | — | 1,421,519 | — |
| Diluted weighted average shares outstanding | 29,636,319 | 28,057,763 | 29,629,462 | 24,954,875 |

- (a) For the three and nine months ended September 27, 2020, as a result of net income for the periods, dilutive earnings per share were calculated using the treasury stock method. The dilutive stock awards have been calculated as 1,421,519 for the three and nine months ended September 27, 2020, related to the outstanding unvested restricted stock units and incremental in-the-money stock options.
- (b) For the three and nine months ended September 29, 2019, as a result of net loss for the period, dilutive stock awards are not presented as this would be antidilutive. Had there been net income for the periods, the dilutive stock awards would have been calculated as 754,820 for the three and nine months ended September 29, 2019, related to outstanding unvested restricted stock units and incremental in-the-money stock options.

8. Segmented information

General description

During the nine months ended September 27, 2020, the Company operated and managed by geographic region in the United States, Mexico and China, which are our operating and reportable segments. Commencing in the three months ended June 28, 2020, China is no longer included as a reportable segment. During the three months ended March 29, 2020, the Company completed final shipments for customers serviced in our Chinese manufacturing facility and the relocation of the equipment to our other North American sites. We utilize each reportable segment’s contribution (revenue minus operating expenses, excluding unrealized foreign exchange gain (loss) on unsettled forward foreign exchange contracts, corporate allocations and restructuring expenses) to monitor reportable segment performance. Contribution by country is utilized by the chief operating decision-maker (defined as the Chief Executive Officer) as the indicator of reportable segment performance, as it reflects costs which our operating segment management are directly responsible for. Intersegment adjustments reflect intersegment sales that are generally recorded at prices that approximate arm’s-length transactions.

In assessing the performance of the reportable segments, management attributes site revenue to the reportable segment that ships the product to the customer, irrespective of the product's destination. Information about the reportable segments is as follows:

| | Three months ended | | Nine months ended | |
|--|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 27, 2020 | September 29, 2019 | September 27, 2020 | September 29, 2019 |
| Revenue | | | | |
| Mexico | \$ 61,625 | \$ 57,328 | \$ 183,791 | \$ 182,424 |
| China | — | 8,092 | 4,206 | 22,541 |
| U.S. | 38,227 | 27,426 | 103,744 | 86,448 |
| Total | \$ 99,852 | \$ 92,846 | \$ 291,741 | \$ 291,413 |
| Intersegment revenue | | | | |
| Mexico | \$ (136) | \$ (550) | \$ (2,706) | \$ (1,293) |
| China | — | (3,580) | (3,302) | (7,687) |
| U.S. | (169) | (34) | (642) | (166) |
| Total | \$ (305) | \$ (4,164) | \$ (6,650) | \$ (9,146) |
| Net external revenue | | | | |
| Mexico | \$ 61,489 | \$ 56,778 | \$ 181,085 | \$ 181,131 |
| China | — | 4,512 | 904 | 14,854 |
| U.S. | 38,058 | 27,392 | 103,102 | 86,282 |
| Total segment revenue (which also equals consolidated revenue) | \$ 99,547 | \$ 88,682 | \$ 285,091 | \$ 282,267 |
| Segment contribution | | | | |
| Mexico | \$ 5,334 | \$ 4,815 | \$ 16,297 | \$ 15,456 |
| China | — | 1,313 | (2) | 3,012 |
| U.S. | 2,521 | 2,191 | 7,753 | 5,378 |
| Total | \$ 7,855 | \$ 8,319 | \$ 24,048 | \$ 23,846 |
| Corporate expenses | 3,725 | 5,962 | 14,377 | 17,227 |
| Restructuring charges | 871 | 6,454 | 525 | 8,624 |
| Change in fair value of warrant liability | 133 | (858) | 15 | (919) |
| Change in fair value of contingent consideration | — | — | — | (3,050) |
| Unrealized foreign exchange gain on unsettled forward exchange contracts | (262) | — | (720) | — |
| Interest expense | 1,941 | 2,679 | 6,021 | 8,349 |
| Income (loss) before income taxes | \$ 1,447 | \$ (5,918) | \$ 3,830 | \$ (6,385) |
| Three months ended September 27, 2020 | Mexico | U.S. | China | Total |
| Market Sector: | | | | |
| Test and Measurement | \$ 147 | \$ 8,019 | \$ — | \$ 8,166 |
| Retail and Payment Systems | 10,295 | — | — | 10,295 |
| Telecom, Networking and Communications | 2,755 | 2,021 | — | 4,776 |
| Medical and Safety | 7,072 | 4,198 | — | 11,270 |
| Industrial IoT, Power and Clean Technology | 29,629 | 7,387 | — | 37,016 |
| Semiconductors | 11,591 | 4,436 | — | 16,027 |
| Avionics, Aerospace and Defense | — | 11,997 | — | 11,997 |
| Segment Revenue | 61,489 | 38,058 | — | 99,547 |
| Revenue by category | Mexico | U.S. | China | Total |
| Point in time | \$ 1,142 | \$ 3,697 | \$ — | \$ 4,839 |
| Over time | 60,347 | 34,361 | — | 94,708 |
| Total Revenue | 61,489 | 38,058 | — | 99,547 |

| Three months ended September 29, 2019 | Mexico | U.S. | China | Total |
|--|----------------|----------------|---------------|----------------|
| Market Sector: | | | | |
| Test and Measurement | \$ 534 | \$ 8,287 | \$ — | \$ 8,821 |
| Retail and Payment Systems | 10,460 | — | — | 10,460 |
| Telecom, Networking and Communications | 3,986 | 1,393 | 4,192 | 9,571 |
| Medical and Safety | 7,861 | 2,637 | 40 | 10,538 |
| Industrial IoT, Power and Clean Technology | 26,610 | 9,851 | 280 | 36,741 |
| Semiconductors | 7,327 | — | — | 7,327 |
| Avionics, Aerospace and Defense | — | 5,224 | — | 5,224 |
| Segment Revenue | <u>56,778</u> | <u>27,392</u> | <u>4,512</u> | <u>88,682</u> |
| Revenue by category | | | | |
| Point in time | \$ 492 | \$ 2,223 | \$ 871 | \$ 3,586 |
| Over time | 56,286 | 25,169 | 3,641 | 85,096 |
| Total Revenue | <u>56,778</u> | <u>27,392</u> | <u>4,512</u> | <u>88,682</u> |
| Nine months ended September 27, 2020 | | | | |
| Market Sector: | | | | |
| Test and Measurement | \$ 724 | \$ 24,632 | \$ — | \$ 25,356 |
| Retail and Payment Systems | 29,368 | — | — | 29,368 |
| Telecom, Networking and Communications | 7,554 | 9,035 | 714 | 17,303 |
| Medical and Safety | 23,498 | 9,693 | 130 | 33,321 |
| Industrial IoT, Power and Clean Technology | 88,102 | 23,217 | 60 | 111,379 |
| Semiconductors | 31,839 | 5,589 | — | 37,428 |
| Avionics, Aerospace and Defense | — | 30,936 | — | 30,936 |
| Segment Revenue | <u>181,085</u> | <u>103,102</u> | <u>904</u> | <u>285,091</u> |
| Revenue by category | | | | |
| Point in time | \$ 2,192 | \$ 6,117 | \$ 452 | \$ 8,761 |
| Over time | 178,893 | 96,985 | 452 | 276,330 |
| Total Revenue | <u>181,085</u> | <u>103,102</u> | <u>904</u> | <u>285,091</u> |
| Nine months ended September 29, 2019 | | | | |
| Test and Measurement | \$ 4,968 | \$ 28,941 | \$ — | \$ 33,909 |
| Retail and Payment Systems | 35,538 | — | — | 35,538 |
| Telecom, Networking and Communications | 11,493 | 5,784 | 11,076 | 28,353 |
| Medical and Safety | 24,362 | 9,393 | 481 | 34,236 |
| Industrial IoT, Power and Clean Technology | 84,389 | 25,122 | 3,297 | 112,808 |
| Semiconductors | 20,381 | 16 | — | 20,397 |
| Avionics, Aerospace and Defense | — | 17,026 | — | 17,026 |
| Segment Revenue | <u>181,131</u> | <u>86,282</u> | <u>14,854</u> | <u>282,267</u> |
| Revenue by category | | | | |
| Point in time | \$ 1,708 | \$ 5,321 | \$ 946 | \$ 7,975 |
| Over time | 179,423 | 80,961 | 13,908 | 274,292 |
| Total Revenue | <u>181,131</u> | <u>86,282</u> | <u>14,854</u> | <u>282,267</u> |

Certain customers were reclassified from the Test and Measurement sector to the Industrial IoT, Power and Clean Technology sector and Semiconductors sector, Avionics, Aerospace and Defense sector to Medical and Safety sector during the three months and nine months ended September 27, 2020. The comparative three and nine month periods have been adjusted to conform to this classification.

Additions to property, plant and equipment

The following table contains additions, including those acquired through capital leases, to property, plant and equipment for the three and nine months ended:

| | Three months ended | | Nine months ended | |
|---------------------|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 27, 2020 | September 29, 2019 | September 27, 2020 | September 29, 2019 |
| U.S. | \$ 676 | \$ 446 | \$ 1,595 | \$ 963 |
| Mexico | 763 | 859 | 1,249 | 2,212 |
| China | 3 | 98 | 5 | 152 |
| Segment total | 1,442 | 1,403 | 2,849 | 3,327 |
| Corporate and other | 5 | — | 8 | 24 |
| Total | <u>\$ 1,447</u> | <u>\$ 1,403</u> | <u>\$ 2,857</u> | <u>\$ 3,351</u> |

Property, plant and operating lease right of use assets (a)

| | September 27, 2020 | December 29, 2019 |
|---------------------|-----------------------|----------------------|
| U.S. | \$ 19,058 | \$ 16,904 |
| Mexico | 10,125 | 10,970 |
| China | — | 670 |
| Segment total | 29,183 | 28,544 |
| Corporate and other | 111 | 96 |
| Total | <u>\$ 29,294</u> | <u>\$ 28,640</u> |

Other long term segment assets (b)

| | September 27, 2020 | December 29, 2019 |
|---------------------|-----------------------|----------------------|
| U.S. | \$ 8,458 | \$ 9,273 |
| Mexico | 20,291 | 22,179 |
| China | — | — |
| Segment total | 28,749 | 31,452 |
| Corporate and other | 742 | 859 |
| Total | <u>\$ 29,491</u> | <u>\$ 32,311</u> |

Total segment assets (a)

| | September 27, 2020 | December 29, 2019 |
|---------------------|-----------------------|----------------------|
| U.S. | \$ 132,313 | \$ 112,789 |
| Mexico | 101,212 | 93,349 |
| China | — | 6,694 |
| Segment total | 233,525 | 212,832 |
| Corporate and other | 552 | 547 |
| Total | <u>\$ 234,077</u> | <u>\$ 213,379</u> |

- (a) Property, plant and equipment information is based on the principal location of the asset.
(b) Includes Goodwill, Intangible assets, deferred income taxes and deferred financing costs.

Geographic revenue

The following table contains geographic revenue based on our customer invoicing location, for the nine months ended September 27, 2020 and September 29, 2019.

| | Three months ended | | Nine months ended | |
|--------|-----------------------|-----------------------|-----------------------|-----------------------|
| | September 27, 2020 | September 29, 2019 | September 27, 2020 | September 29, 2019 |
| U.S. | \$ 95,381 | \$ 83,276 | \$ 270,303 | \$ 260,210 |
| Canada | 4,166 | 3,916 | 13,834 | 13,686 |
| China | — | 1,490 | 954 | 8,371 |
| Total | \$ 99,547 | \$ 88,682 | \$ 285,091 | \$ 282,267 |

Significant customers and concentration of credit risk

Sales of the Company's products are concentrated in certain cases among specific customers in the same industry. The Company is subject to concentrations of credit risk in trade receivables. The Company considers concentrations of credit risk in establishing the allowance for doubtful accounts and believes the recorded allowances are adequate.

The Company expects to continue to depend upon a relatively small number of customers for a significant percentage of its revenue. In addition to having a limited number of customers, the Company manufactures a limited number of products for each customer. If the Company loses any of its larger customers or any product line manufactured for one of its larger customers, it could experience a significant reduction in revenue. Also, the insolvency of one or more of its larger customers or the inability of one or more of its larger 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 the business, financial condition and results of operations.

During the nine months ended September 27, 2020, two customers exceeded 10% of total revenue, comprising of 22.7% of total revenue across all geographic segments. During the nine months ended September 29, 2019, one customer exceeded 10% of total revenue, comprising of 13.4% of total revenue across all geographic segments.

As of September 27, 2020, no customers represented more than 10% of the trade accounts receivable. At December 29, 2019, one customer comprised 10% of the Company's trade accounts receivable. No other customers individually represented more than 10% of total revenue or trade accounts receivable.

9. Derivative financial instruments

During the nine months ended September 27, 2020, the Company entered into forward foreign exchange contracts to reduce its exposure to foreign exchange currency rate fluctuations related to forecasted Mexican peso expenditures. These contracts were effective as hedges from an economic perspective, but do not meet the requirements for hedge accounting under ASC Topic 815 "Derivatives and Hedging". Accordingly, changes in the fair value of these contracts were recognized into net income in the consolidated statement of operations and comprehensive income (loss). The Company had no outstanding forward foreign exchange contracts in the first nine months of 2019.

The following table presents a summary of the outstanding foreign currency forward contracts as at September 27, 2020:

| Currency | Buy/Sell | Foreign Currency Amount | Notional Contract Value in USD |
|--------------|----------|-------------------------|--------------------------------|
| Mexican Peso | Buy | 180,000 MXN | \$ 7,212 |

The unrealized gain recognized in earnings as a result of revaluing the instruments to fair value on September 27, 2020 for the nine months period ended was \$20 (September 29, 2019— \$Nil) which was included in cost of sales in the interim consolidated statement of operations and comprehensive income (loss). Fair value is determined using the market approach with valuation based on market observables (Level 2 quantitative inputs in the hierarchy set forth under ASC 820 "Fair Value Measurements").

The average contract and mark-to-market rates for outstanding forward foreign exchange contracts were as follows:

| | September 27, 2020 | December 29, 2019 |
|--------------------------------------|-----------------------|----------------------|
| Average USD:PESO contract rate | 24.96 | N/A |
| Average USD:PESO mark-to-market rate | 22.69 | N/A |

The derivative assets were \$720 as at September 27, 2020 (September 29, 2019 –Nil) which reflected the fair market value of the unsettled forward foreign exchange contracts. There was no derivative liability as at September 27, 2020 or September 29, 2019.

10. Restructuring Charges

In July 2020, the Company executed its plans to reduce headcount, which impacted 307 full-time equivalents (“FTEs”), representing 287 FTEs in its Zacatecas facility and 20 FTEs located in the U.S. A restructuring charge of \$1,163 was recorded during the three months ended September 27, 2020. The remaining restructuring accrual as at September 27, 2020 was \$194 and is scheduled to be paid by the end of December 2020.

Dongguan facility closure

In September 2019, the Company announced its plans to close its Dongguan manufacturing facility in China, concurrent with the expiration of the facility lease in December 2019, which was extended to February 2020. The closure was formally approved by the Board of Directors in September 2019. A restructuring charge of \$5,000 was recorded in the twelve months ended December 29, 2019 relating to the announced planned closure. The closure of the Dongguan facility resulted in a reduced labor force by approximately 137 employees. The employee group was notified of the closure in the last week of September 2019. The closure of the Dongguan facility and majority of the cash outflows associated with severance and other exit costs which was substantially completed by the end of the first quarter of 2020. During the nine months ended September 27, 2020, restructuring recoveries were recorded of \$753 primarily related to shipments and cash payments received on previously provisioned Dongguan inventory, in addition to restructuring reversals as actual payments were less than anticipated. Remaining activities include a small number of support staff performing administrative duties, professional services to be rendered with respect to the closure activities, taxes and duties to be settled in addition to severance payments. Substantially all of the costs are anticipated to be spent by the third quarter of 2020. Manufacturing by the Company of certain products previously manufactured at the Dongguan facility has been transferred to the Company’s other manufacturing facilities. As at September 27, 2020, the Company had \$17 of accrued restructuring charges remaining related to Dongguan to be paid by the end of the fourth quarter of 2020 primarily related to employee severance and legal fees.

Restructuring Liability

| | Termination benefits and other exit costs |
|---|--|
| Balance as at December 29, 2019 | \$ 1,597 |
| Involuntary employee termination benefits | 1,278 |
| Provisions reversed/unutilized | (753) |
| Payments—Dongguan severance and other exit cost payment | (549) |
| Payments—(U.S., Canada and Mexico) | (1,209) |
| At September 27, 2020 | <u>\$ 364</u> |

11. Commitments

Purchase obligations not recorded on the balance sheet as at September 27, 2020 consist of open non-cancellable purchase orders (PO) for raw materials for \$7,708, which are expected to be paid within 12 months of the PO issue date. Purchase obligations not recorded on the balance sheet as at December 29, 2019, consisted of open non-cancellable purchase orders for raw materials for \$25,866 to be paid within 12 months of the PO issue date.

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

Where we say “we”, “us”, “our”, the “Company” or “SMTC”, we mean SMTC Corporation or SMTC Corporation and its subsidiaries, as the context may require. Where we refer to the “industry”, we mean the electronics manufacturing services industry.

You should read this Management’s Discussion and Analysis of Financial Condition and Results of Operations (“MD&A”) in combination with the accompanying unaudited interim consolidated financial statements and related notes as well as the audited consolidated financial statements and the accompanying notes to the consolidated financial statements prepared in accordance with accounting principles generally accepted in the United States (“U.S. GAAP”) included within the Company’s Annual Report on Form 10-K filed on March 13, 2020.

The forward-looking statements in this discussion and elsewhere in this quarterly report, including those regarding the electronics manufacturing services industry, market conditions, our expectations regarding our future performance, liquidity and capital resources, the impact of accounting standards not yet adopted, compliance with financial covenants under our Credit Facilities, future response to and effects of the COVID-19 pandemic, including on our employees, continued operations, customers suppliers, logistics providers, implementation of protective measures, public policy response to the COVID-19 pandemic including legislation or restrictions, our expectations regarding customer concentration, our expectations regarding timing and mitigation of the identified material weakness in internal control over financial reporting, and other non-historical statements include numerous risks and uncertainties, some of which are as described in the “Risk Factors” section in the Annual Report on Form 10-K filed on March 13, 2020, as updated by Item 1A in Part II of this quarterly report. Certain statements in this MD&A contain words such as “could”, “expects”, “may”, “anticipates”, “believes”, “intends”, “estimates”, “plans”, “envisions”, “seeks” and other similar language and are considered forward looking statements or information under applicable securities laws. These statements are based on our current expectations, estimates, forecasts and projections about the operating environment, economies and markets in which we operate. These statements are subject to important assumptions, risks and uncertainties, which are difficult to predict and the actual outcome may be materially different. Except as required by applicable law, we do not intend to update these forward-looking statements after the date of this quarterly report, even though our situation may change in the future. All forward-looking statements attributable to us are expressly qualified by these cautionary statements.

This MD&A contains discussion in U.S. dollars (US\$) unless specifically stated otherwise.

Background

We are a provider of end-to-end electronics manufacturing services (“EMS”), including product design and engineering services, printed circuit board assembly (“PCBA”), production, enclosure, cable assembly, precision metal fabrication, systems integration and comprehensive testing services, configuration to order (“CTO”), build to order (“BTO”) and direct order fulfillment (“DOF”). We operate more than 50 manufacturing and assembly lines in over 555,000 square feet of production space worldwide at strategically located facilities in the United States and Mexico, that provide local support, flexibility, fast turn around and delivery times, and low-cost, volume manufacturing capabilities, as well as new product integration (“NPI”) services, to our global customers. Our services extend over the entire electronic product life cycle from new product development and NPI through to growth, maturity and end of life phases. As of September 27, 2020, we had 3,207 employees of which 2,616 were full time and contract employees.

COVID-19 Update

We continue to monitor the global pandemic and spread of COVID-19 and take steps to mitigate the potential risks to us posed by its spread and related circumstances and impacts. While our business operations have generally performed as expected during the first nine months of 2020, the COVID-19 pandemic continues to represent significant uncertainty for the remainder of the year and into fiscal 2021, and has the potential to negatively impact the results of our operations, cash flows and financial position.

Workplace Safety

The health and safety of our employees is a top priority for us. All of our facilities remain in operation and we have progressively implemented measures to safeguard our employees from COVID-19 infection and exposure, in accordance with guidelines established by the Centers for Disease Control, other governmental requirements, and our own safety standards. These consist of policies, procedures, protocols, and guidance related to, among other things, COVID-19 symptom awareness, effective hygiene practices, travel restrictions, visitor restrictions, social distancing, face covering expectations, temperature and health screening, work-from-home requirements, employee infection assessments, close contact tracing, enhanced workplace cleaning, and large-scale decontamination. These efforts will continue as requirements change, new risks are identified, and infections impact us. We anticipate incurring higher direct labor charges in the fourth quarter of 2020 as a result of the continuation of these efforts.

In addition, in all geographies in which we operate, regulatory authorities at some point have imposed restrictions regarding the conduct of business and people movement to safeguard its citizens. To address these requirements, we are in continuous communication with our employees and union representatives, in addition to government and state representatives where our manufacturing facilities reside. If one or more of our manufacturing facilities were temporarily closed or had their operations limited, or customers pushed out demand due to the pandemic, this would have a material impact on our operations.

Supply Chain

Our suppliers may face challenges in maintaining an adequate workforce or securing materials from their own suppliers as a result of the COVID-19 pandemic. As a result, we may experience an inability to procure certain components and materials on a timely basis, or increased shipping costs or lead times. We continue to take steps to coordinate with our suppliers and validate our suppliers' ability to deliver to us on time, which may also be affected by the impact of the COVID-19 pandemic on their own financial condition. Despite these efforts it is possible that an extended pandemic could disrupt the operation of our supply chain.

Customers

We are also in close contact with our customers to understand the impact of the COVID-19 pandemic on their businesses and the resulting potential impact on our business. The COVID-19 pandemic has introduced volatility and uncertainty to all of our customers, which has required us to react and respond. Although many of the products we manufacture for our customers are deemed essential, the COVID-19 pandemic may impact demand for our customers' products, which could impact our production schedules. While the COVID-19 pandemic has negatively impacted some of our customers and, therefore, our business with them, we have experienced opportunities with new and existing customers, to manufacture products that may be used in the effort to combat the effects of COVID-19.

Liquidity

We incurred an additional \$1.3 million in COVID-19 related expenses in the third quarter primarily due to the retention of temporary replacement labor, additional sanitation, cleaning and disinfection of facilities, personal protective equipment and related supplies, costs related to facilitating social distancing and logistics costs associated with expediting inventory purchases from existing and new sources. With respect to liquidity, we continue to evaluate and take actions to reduce costs and spending across our Company, including pausing all non-essential new hiring and new programs and reducing our capital expenditures. While we are unable to determine or predict the nature, duration or scope of the overall impact the COVID-19 pandemic will have on our business, results of operations, liquidity or capital resources, we continue to actively monitor the situation and may take further actions that alter our business operations to comply with requirements by federal, state or local authorities or that we determine are in the best interests of our employees, customers, suppliers, and stockholders.

As at September 27, 2020, we had \$30.5 million available to borrow under our PNC Facility (as described and defined below) after deducting the current borrowing base conditions and subject to debt covenants. .

Results of Operations

The unaudited interim consolidated financial statements of SMTC are prepared in accordance with U.S. GAAP.

Quarter ended September 27, 2020 compared with the quarter ended September 29, 2019:

The following table sets forth summarized operating results in millions of US\$ for the periods indicated:

| | Three months ended September 27, 2020 | | Three months ended September 29, 2019 | | Change 2019 to 2020 | |
|---|--|-------|--|-------|------------------------|--------|
| | \$ | % | \$ | % | \$ | % |
| Revenue | 99.5 | 100.0 | 88.7 | 100.0 | 10.8 | 12.2 |
| Cost of sales | 88.4 | 88.8 | 79.8 | 90.0 | 8.6 | 10.8 |
| Gross profit | 11.1 | 11.2 | 8.9 | 10.0 | 2.2 | 24.7 |
| Selling, general and administrative expenses | 6.7 | 6.7 | 6.6 | 7.4 | 0.1 | 1.5 |
| Restructuring charges | 0.9 | 0.9 | 6.4 | 7.2 | (5.5) | (85.9) |
| Operating income (loss) | 3.5 | 3.5 | (4.1) | (4.6) | 7.6 | 185.4 |
| Fair value measurement loss (gain) on warrant liability | 0.1 | 0.1 | (0.9) | (1.0) | 1.0 | 111.1 |
| Interest expense | 2.0 | 2.0 | 2.7 | 3.0 | (0.7) | (25.9) |
| Income (loss) before income taxes | 1.4 | 1.4 | (5.9) | (6.7) | 7.3 | 123.7 |
| Income tax expense (recovery) | | | | | | |
| Current | 0.3 | 0.3 | (0.1) | (0.1) | 0.4 | 400.0 |
| Deferred | (0.1) | (0.1) | (0.1) | (0.1) | — | — |
| | 0.2 | 0.2 | (0.2) | (0.2) | 0.4 | 200.0 |
| Net income (loss) | 1.2 | 1.2 | (5.7) | (6.4) | 6.9 | 121.9 |

Revenue by Industry Sector

| Industry Sector | Three months ended September 27, 2020 | | Three months ended September 29, 2019 | | Change | |
|--|--|--------------|--|--------------|-------------|-------------|
| | \$ | % | \$ | % | \$ | % |
| Test and Measurement | 8.1 | 8.1 | 8.8 | 9.9 | (0.7) | (8.0) |
| Retail and Payment Systems | 10.3 | 10.4 | 10.6 | 12.0 | (0.3) | (2.8) |
| Telecom, Networking and Communications | 4.8 | 4.8 | 9.6 | 10.8 | (4.8) | (50.0) |
| Medical and Safety | 11.3 | 11.4 | 10.5 | 11.8 | 0.8 | 7.6 |
| Industrial IoT, Power and Clean Technology | 37.0 | 37.2 | 36.7 | 41.4 | 0.3 | 0.8 |
| Semiconductors | 16.0 | 16.1 | 7.3 | 8.2 | 8.7 | 119.2 |
| Avionics, Aerospace and Defense | 12.0 | 12.1 | 5.2 | 5.9 | 6.8 | 130.8 |
| Total | 99.5 | 100.0 | 88.7 | 100.0 | 10.8 | 12.2 |

Certain customers were reclassified from the Test and Measurement sector to the Industrial IoT, Power and Clean Technology sector and Semiconductors sector, Avionics, Aerospace and Defense sector to Medical and Safety sector during the three months ended September 27, 2020. The comparative three period has been adjusted to conform to this classification.

Total revenue increased \$10.8 million to \$99.5 million for the third quarter of 2020 from \$88.7 million in the same period in the prior year due to increased demand in the commercial avionics, test and measurement and semiconductor programs, among others, offset by customer disengagement in China due to the Dongguan facility closure in the third quarter of 2020, along with order rescheduling from other North America customers in the latter part of the third quarter of 2020. We believe this resulted in part from the COVID-19 pandemic and our customers modifying their requirements in response to shifting demand of their respective end customers.

Revenue decreased \$0.7 million in the test and measurement sector compared to the third quarter of 2019, primarily due to reduced volumes from one customer, offset by increased volumes from one customer, all serviced in the U.S.

Revenue decreased \$0.3 million in the retail and payment systems sector compared to the third quarter of 2019, primarily due to decreased volume from two customers, offset by increased volume from one customer, all serviced in Mexico.

Revenue decreased \$4.8 million in the telecom, networking and communications sector compared to the third quarter of 2019, primarily due to one customer serviced in the Mexico experiencing reduced volumes due to the customer's program transitioning to end-of-life, and two customers disengaging in China due to the Dongguan facility closure.

Revenue increased \$0.8 million in the medical and safety sector compared to the third quarter of 2019, primarily due to increased volumes with one customer serviced in Mexico and one new customer serviced in the U.S., offset by decreased volumes with two customers serviced in Mexico.

Revenue increased \$0.3 million in the industrial IoT, power and clean technology sector compared to the third quarter of 2019, primarily due to increased volume from one customer serviced in Mexico, offset by decreased volumes from two customers serviced in the U.S. and two customers serviced in Mexico.

Revenue increased \$8.7 million in the semiconductors sector compared to the third quarter of 2019, due to increased volume from two customers serviced in Mexico, and one new customer serviced in the U.S.

Revenue increased \$6.8 million in the avionics, aerospace and defense sector compared to the third quarter of 2019, due to the addition of one new customer, volume increases with three customers, offset by volume decreases with another customer, all serviced in the U.S.

Revenue by Geography

During the third quarter of 2020, 61.8% of our revenue was attributable to production from our operations in Mexico and 38.2% of our revenue was attributable to production from our operations in the U.S. During the third quarter of 2019, 64.0% of our revenue was attributable to production from our operations in Mexico, 30.9% of our revenue was attributable to production from our operations in the U.S. and 5.1% of our revenue was attributable to production from our operations in China. Following the closure of our Dongguan manufacturing facility in China, manufacturing of certain products previously manufactured at that facility has been transferred to the Company's other manufacturing facilities..

Additional Revenue Information

We recorded approximately \$4.8 million and \$3.6 million of revenue from sales of raw materials inventory to customers during the third quarter of 2020 and the third quarter of 2019, respectively. The Company purchases raw materials based on customer purchase orders. When a customer requires an order to be altered or changed, the customer is generally obligated to purchase the original on-order raw material at cost, to the extent the materials are not consumed within a specified period.

The Company's ten largest customers represented 60.3% of revenue during the third quarter of 2020, compared with 53.1% in the third quarter of 2019. Revenue from the two largest customers during the third quarter of 2020 was \$11.6 million representing 11.7% and \$11.0 million representing 11.1% of total revenue. This compares with revenue from the largest customer during the third quarter of 2019 of \$10.9 million representing 12.3 % of total revenue. No other customers represented more than 10% of revenue in either period.

Gross Profit

Gross profit for the third quarter of 2020 increased by \$2.2 million to \$11.1 million or 11.2% of revenue compared with \$8.9 million or 10.0% of revenue for the same period in 2019. When excluding unrealized foreign exchange gain on unsettled forward contracts ,amortization of intangible assets and COVID-19 related expenses, the adjusted gross profit was \$12.5 million or 12.6% of revenue for the third quarter of 2020 compared with \$10.8 million or 12.1% of revenue for the third quarter of 2019. The increase in gross profit percentage is primarily due to headcount reductions, resulting in labor efficiencies.

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased to \$6.7 million in the third quarter of 2020 from \$6.6 million in the same period in 2019.

Restructuring Charges

During the third quarter of 2020, we recorded restructuring expenses of \$1.2 million primarily related to the reduction of 307 full-time equivalents ("FTEs"), at our Zacatecas, Mexico facility, partially offset by restructuring provision reversals of \$0.3 million previously included for the Dongguan facility. During the third quarter of 2019, we accrued restructuring charges of \$5.5 million related to the Company's previously announced closure of business operations in Dongguan, China, in addition to \$0.9 million related to the reduction of 19 FTEs in the U.S, 4 FTEs in Canada and 89 FTEs and contract employees in Mexico. The restructuring charges related to the Dongguan facility included \$1.4 million of severance charges related to the reduction of 137 FTEs and other facility closure activities, accrued tax and duties of \$0.2 million, and equipment decommissioning and facility charges of \$0.4 million. In

addition, the restructuring charges included a \$1.7 million write down of accounts receivable, a \$1.5 million write down of inventory and \$0.3 million write down of property, plant and equipment.

As at September 27, 2020, the Company had \$0.4 million of accrued restructuring charges remaining related to Dongguan for employee severance, and legal fees and U.S. employee severance to be paid by the end of the fourth quarter of 2020.

Interest Expense

Interest expense decreased to \$2.0 million in the third quarter of 2020 compared to \$2.7 million in the same period in 2019, respectively. The decrease primarily resulted from the pay down of the Term Loan B Facility in addition to lower average debt balance in the third quarter of 2020 compared to the same period in 2019. The weighted average interest rates with respect to the debt on our PNC and TCW Facilities was 6.94%. The weighted average interest rates for the same period in the prior year was 12.2%.

Income Tax Expense

The Company recorded current income tax expense of \$0.3 million and \$0.1 million for the third quarters of 2020 and 2019, in connection with U.S. state taxes and taxes on profits in certain foreign jurisdictions, and deferred income tax benefit of \$0.1 million in the third quarter of 2020 and 2019, in connection with temporary differences related to the Mexican operations.

Non-GAAP Financial Measures

To supplement our consolidated financial statements, which are prepared and presented in accordance with U.S. GAAP, we use the following non-GAAP financial measures: Adjusted Gross Profit, EBITDA, Adjusted EBITDA and Adjusted Net Income (collectively the “Non-GAAP Financial Measures”). We believe that these Non-GAAP Financial Measures, when used in conjunction with GAAP financial measures, provide useful information about operating results, enhance the overall understanding of past financial performance and future prospects, and allow for greater transparency with respect to the key metrics we use in our financial and operational decision making, as they exclude the effects of items that may not be indicative of, or are unrelated to, our underlying operating results, such as expenses related to the COVID-19 pandemic. The Company’s management believes that adjusting for the additional temporary costs attributable to the COVID-19 pandemic allows for a better comparison of the Company’s performance to prior periods, which is consistent with our recent amendments to the financial covenants in our financing agreements. These non-GAAP measures are used by the Company’s management to manage and monitor the Company’s performance, and also frequently used by analysts, investors and other interested parties to evaluate companies in our industry. The presentation of this financial information is not intended to be considered in isolation or as a substitute for, or superior to, the financial information prepared and presented in accordance with U.S. GAAP, and they should not be construed as an inference that our future results will be unaffected by any items adjusted for in these non-GAAP measures. In evaluating these non-GAAP measures, you should be aware that in the future we may incur expenses that are the same as or similar to some of those adjusted in this presentation. The Non-GAAP Financial Measures that we use are not necessarily comparable to similarly titled measures used by other companies due to different methods of calculation.

Net Income and Adjusted Net Income Reconciliation

Adjusted Net Income, a non-GAAP financial measure, is defined as Net Income before amortization of intangible assets, restructuring charges, stock-based compensation, fair value adjustment of warrant liability, merger and acquisition related expenses and unrealized foreign exchange gains and losses on unsettled forward foreign exchange contracts and COVID-19 related expenses. Management presents Adjusted Net Income, as it is believed the information is useful to investors in understanding and evaluating our operating results as it aligns the net income (loss) with those adjustments made to EBITDA and gross profit.

Below is the reconciliation of Net Income to Adjusted Net Income (in thousands):

| | September 27, 2020 | September 29, 2019 |
|---|-----------------------|-----------------------|
| Net income (loss) | \$ 1,243 | \$ (5,734) |
| Add: | | |
| Amortization of intangible assets | 354 | 1,844 |
| Restructuring charges | 871 | 6,454 |
| Stock based compensation | 158 | 353 |
| Fair value adjustment of warrant liability | 133 | (858) |
| Merger and acquisitions related expenses | — | 68 |
| COVID-19 related expenses (1) | 1,348 | — |
| Unrealized foreign exchange gain on unsettled forward foreign exchange contracts | (261) | — |
| Adjusted net income | <u>\$ 3,846</u> | <u>\$ 2,127</u> |

- (1) Includes costs attributable to the COVID-19 pandemic, including retention of temporary replacement labor, additional sanitation, cleaning and disinfection of facilities, personal protective equipment and related supplies, costs associated with facilitating social distancing and logistics costs associated with expediting inventory purchases from existing and new sources.

Net income increased to \$1.2 million from a \$5.7 million loss in the third quarter of 2020 and 2019, respectively. This was due to increased gross profit, partially driven by an unrealized foreign exchange gain on unsettled forward contracts and a reduction in amortization of intangible assets and headcount reductions. Also contributing was a decrease in interest expense and decreased restructuring cost recorded in the third quarter of 2020 over the same period in the prior year. The net income in the third quarter of 2020 was partially offset by \$1.3 million of COVID-19 related expenses not incurred for the same period in the prior year. When excluding the items in the reconciliation above, Adjusted Net Income increased \$1.7 million in the third quarter of 2020 over the same period in the prior year.

Gross Profit and Adjusted Gross Profit Reconciliation

Adjusted Gross Profit, a non-GAAP financial measure, is defined as gross profit exclusive of unrealized foreign exchange gains or losses on unsettled forward foreign exchange contracts and the amortization of intangible assets. The Company calculates an adjusted gross profit amount as we consider gross profit exclusive of such unrealized foreign exchange gains or losses on unsettled forward foreign exchange contracts to be a meaningful measure as it is non-cash and management does not consider the mark-to-market valuation reflective of operating performance in the current period. Management also excludes the impact of intangible assets amortization as these charges are non-cash in nature and are not believed to be reflective of operating performance. Management also excludes COVID-19 related expenses as it believes these costs are not reflective of normal operations due to pandemic. We also believe adjusted gross profit provides useful information to investors in understanding and evaluating our operating results in the same manner as management.

Below is the reconciliation from the financial statement presentation of gross profit to the non-GAAP measure of adjusted gross profit (in thousands):

| | Three months ended September 27, 2020 | Three months ended September 29, 2019 |
|---|---|---|
| Gross profit | \$ 11,102 | \$ 8,906 |
| Add: | | |
| Unrealized foreign exchange gain on unsettled forward exchange contracts | (261) | — |
| Amortization of intangible assets | 354 | 1,844 |
| COVID-19 related expenses (1) | 1,348 | — |
| Adjusted gross profit | <u>\$ 12,543</u> | <u>\$ 10,750</u> |
| Adjusted gross profit percentage | <u>12.6%</u> | <u>12.1%</u> |

- (1) Includes costs attributable to the COVID-19 pandemic, including retention of temporary replacement labor, additional sanitation, cleaning and disinfection of facilities, personal protective equipment and related supplies, costs associated with facilitating social distancing and logistics costs associated with expediting inventory purchases from existing and new sources.

EBITDA and Adjusted EBITDA Reconciliation

EBITDA and Adjusted EBITDA, non-GAAP financial measures, are defined as earnings before interest, taxes, depreciation and amortization, with Adjusted EBITDA also excluding restructuring charges, stock-based compensation, unrealized foreign exchange gains and losses on unsettled forward foreign exchange contracts, fair value adjustment of warrant liability and merger and acquisition related expenses and COVID-19 related expenses. Management presents EBITDA and Adjusted EBITDA, as they are utilized by management to monitor performance against budget as well as compliance with bank covenants. We also believe EBITDA and Adjusted EBITDA provide useful information to investors in understanding and evaluating our operating results in the same manner as management.

Below is the reconciliation of net income (loss), the closest GAAP measure, to EBITDA and Adjusted EBITDA (in thousands).

| | Three months ended September 27, 2020 | Three months ended September 29, 2019 |
|---|---|---|
| Net income (loss) | \$ 1,243 | \$ (5,734) |
| Add: | | |
| Depreciation of property, plant and equipment | 1,545 | 1,649 |
| Amortization of intangible assets | 354 | 1,844 |
| Interest | 1,941 | 2,679 |
| Income taxes expense (recovery) | 204 | (184) |
| EBITDA | \$ 5,287 | \$ 254 |
| Add: | | |
| Restructuring charges | 871 | 6,454 |
| Stock based compensation | 158 | 353 |
| Fair value adjustment of warrant liability | 133 | (858) |
| Merger and acquisition related expenses | — | 68 |
| COVID-19 related expenses (1) | 1,348 | — |
| Unrealized foreign exchange gain on unsettled forward exchange contracts | (261) | — |
| Adjusted EBITDA | \$ 7,536 | \$ 6,271 |

- (1) Includes costs attributable to the COVID-19 pandemic, including retention of temporary replacement labor, additional sanitation, cleaning and disinfection of facilities, personal protective equipment and related supplies, costs associated with facilitating social distancing and logistics costs associated with expediting inventory purchases from existing and new sources.

Adjusted EBITDA for three months ended September 27, 2020 increased by \$1.3 million to \$7.5 million compared with \$6.3 million for the same period in 2019 due to the increase in gross profit, partially offset by increased selling, general and administrative expenses.

Nine months ended September 27, 2020, compared with the nine months ended September 29, 2019:

The following table sets forth summarized operating results in millions of US\$ for the periods indicated:

| | Nine months ended September 27, 2020 | | Nine months ended September 29, 2019 | | Change 2019 to 2020 | |
|---|---|-------|---|-------|------------------------|--------|
| | \$ | % | \$ | % | \$ | % |
| Revenue | 285.1 | 100.0 | 282.3 | 100.0 | 2.8 | 1.0 |
| Cost of sales | 253.7 | 89.0 | 255.7 | 90.6 | (2.0) | (0.8) |
| Gross profit | 31.4 | 11.0 | 26.6 | 9.4 | 4.8 | 18.0 |
| Selling, general and administrative expenses | 21.0 | 7.4 | 19.9 | 7.0 | 1.1 | 5.5 |
| Change in fair value of contingent consideration | 0.0 | 0.0 | (3.0) | (1.1) | 3.0 | 100.0 |
| Restructuring charges | 0.5 | 0.2 | 8.6 | 3.0 | (8.1) | (94.2) |
| Operating income | 9.9 | 3.4 | 1.1 | 0.4 | 8.8 | 800.0 |
| Fair value measurement loss (gain) on warrant liability | 0.0 | 0.0 | (0.9) | (0.3) | 0.9 | 100.0 |
| Interest expense | 6.0 | 2.1 | 8.4 | 3.0 | (2.4) | (28.6) |
| Income (loss) before income taxes | 3.9 | 1.3 | (6.4) | (2.3) | 10.3 | 160.9 |
| Income tax expense | | | | | | |
| Current | 0.9 | 0.3 | 0.6 | 0.2 | 0.3 | 50.0 |
| Deferred | 0.0 | 0.0 | 0.0 | 0.0 | — | — |
| | 0.9 | 0.3 | 0.6 | 0.2 | 0.3 | 50.0 |
| Net income (loss) | 3.0 | 1.0 | (7.0) | (2.5) | 10.0 | 142.9 |

Revenue by Industry Sector

| Industry Sector | Nine months ended September 27, 2020 | | Nine months ended September 29, 2019 | | Change | |
|--|---|--------------|---|--------------|------------|------------|
| | \$ | % | \$ | % | \$ | % |
| Test and Measurement | 25.4 | 8.9 | 33.9 | 12.0 | (8.5) | (25.1) |
| Retail and Payment Systems | 29.4 | 10.3 | 35.6 | 12.6 | (6.2) | (17.4) |
| Telecom, Networking and Communications | 17.3 | 6.1 | 28.4 | 10.1 | (11.1) | (39.1) |
| Medical and Safety | 33.3 | 11.7 | 34.2 | 12.1 | (0.9) | (2.6) |
| Industrial IoT, Power and Clean Technology | 111.4 | 39.1 | 112.8 | 40.0 | (1.4) | (1.2) |
| Semiconductors | 37.4 | 13.1 | 20.4 | 7.2 | 17.0 | 83.3 |
| Avionics, Aerospace and Defense | 30.9 | 10.8 | 17.0 | 6.0 | 13.9 | 81.8 |
| Total | 285.1 | 100.0 | 282.3 | 100.0 | 2.8 | 1.0 |

Certain customers were reclassified from the Test and Measurement sector to the Industrial IoT, Power and Clean Technology sector and Semiconductors sector, Avionics, Aerospace and Defense sector to Medical and Safety sector during the three months ended September 27, 2020 and six months ended June 28, 2020. The comparative three and nine month periods have been adjusted to conform to this classification.

Total revenue increased \$2.8 million to \$285.1 million for the first nine months of 2020 from \$282.3 million in the same period in the prior year primarily due to some demand gains from commercial avionics and test and measurement programs, among others, and customer disengagement in China due to the Dongguan facility closure in the third quarter of 2019, along with order rescheduling from other North America customers in the latter part of the third quarter of 2020. We believe this resulted in part from the COVID-19 pandemic and our customers modifying their requirements in response to shifting demand of their respective end customers.

Revenue decreased \$8.5 million in the test and measurement sector compared to the first nine months of 2019, primarily due to reduced volume from one customer serviced in the U.S.

Revenue decreased \$6.2 million in the retail and payment systems sector compared to the first nine months of 2019, primarily due to decreased volume from two customers, offset by increased volume from one customer, all serviced in Mexico.

Revenue decreased \$11.1 million in the telecom, networking and communications sector compared to the first nine months of 2019, primarily due to two customers disengaging in China due to the Dongguan facility closure, one customer serviced in Mexico experiencing reduced volumes due to the customer's program transitioning to end-of-life, and one customer serviced in Mexico with reduced volume, partially offset by one new customer serviced in the U.S.

Revenue decreased \$0.9 million in the medical and safety sector compared to the first nine months of 2019, primarily due to one customer serviced in the U.S. experiencing reduced volumes due to the customer's program transitioning to end-of-life, decreased volume from two customers, partially offset by one new customer serviced in Mexico and two new customers serviced in the U.S.

Revenue decreased \$1.4 million in the industrial IoT, power and clean technology sector compared to the first nine months of 2019, primarily due to decreased volume from four customers (two serviced in Mexico; two serviced in the U.S.), partially offset by increased volume from two customers serviced in Mexico.

Revenue increased \$17.0 million in the semiconductors sector compared to the first nine months of 2019, due to increased volume from three customers serviced in Mexico and one new customer serviced in the U.S.

Revenue increased \$13.9 million in the avionics, aerospace and defense sector compared to the first nine months of 2019, due to volumes increases with two customers, as well as one new customer, offset by volume decreases with one customer, all serviced in the U.S.

Revenue by Geography

During the first nine months of 2020, 63.5% of our revenue was attributable to production from our operations in Mexico, 36.2% of our revenue was attributable to production from our operations in the U.S. and 0.3% of our revenue was attributable to production from our operations in China. During the first nine months of 2019, 64.2% of our revenue was attributable to production from our operations in Mexico, 30.6% of our revenue was attributable to production from our operations in the U.S. and 5.3% of our revenue was attributable to production from our operations in China. Following the closure of our Dongguan manufacturing facility in China, manufacturing of certain products previously manufactured at that facility has been transferred to the Company's other manufacturing facilities.

Additional Revenue Information

We recorded approximately \$8.8 million and \$8.0 million of revenue from sales of raw materials inventory to customers during the first nine months of 2020 and the first nine months of 2019. The Company purchases raw materials based on customer purchase orders. When a customer requires an order to be altered or changed, the customer is generally obligated to purchase the original on-order raw material at cost, to the extent the materials are not consumed within a specified period.

The Company's ten largest customers represented 55.5% of revenue during the first nine months of 2020, compared with 54.0% in the first nine months of 2019. Revenue from the largest customer during the first nine months of 2020 was \$38.2 million representing 13.4% of total revenue. This compares with revenue from the largest customer during the first nine months of 2019 of \$36.7 million representing 13.0% of total revenue. No other customers represented more than 10% of revenue in either period.

Gross Profit

Gross profit for the first nine months of 2020 increased by \$4.8 million to \$31.4 million or 11.0% of revenue compared with \$26.6 million or 9.4% of revenue for the same period in 2019. When excluding unrealized foreign exchange gain on unsettled forward contracts, amortization of intangible assets and COVID-19 related expenses, the adjusted gross profit was \$36.0 million or 12.6% of revenue for the first nine months of 2020 compared with \$32.1 million or 11.4% of revenue for the first nine months of 2019. This was due primarily to higher gross profit due to product mix and lower variable manufacturing expenses in addition to headcount reductions resulting in labor efficiencies.

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased to \$21.0 million in the first nine months of 2020 from \$19.9 million in the same period in 2019, mainly due to increased professional services rendered related to additional compliance obligations under the Sarbanes-Oxley Act of 2002, as well as new headcount hired in the first nine months of 2020.

Change in fair value of contingent consideration

During the first nine months of 2019, it was determined that there was no fair value of the contingent consideration liability, and that no obligation existed resulting in a recognized gain of \$3.1 million. The contingent consideration liability was initially recognized at fair value in the fourth quarter of 2018 and relates to a contingent earn-out payment associated with the acquisition of MC Assembly. The fair value estimate under purchase accounting of \$3.1 million was derived from a multiple of earnings based on MC Assembly's forecasted twelve-month earnings for the period ended September 29, 2019. Based on actual earnings, the contingent consideration liability was considered resolved and no longer payable as at September 29, 2019. No contingent consideration existed as at September 27, 2020.

Restructuring Charges

During the first nine months of 2020, we recorded restructuring expenses of \$1.3 million primarily related to the reduction of 307 FTEs, offset by restructuring recoveries of \$0.8 million included in the Dongguan facility.

During the first nine months of 2019, \$8.6 million of restructuring charges were incurred related to the reduction of 137 FTEs in China, 28 FTEs in U.S., 4 FTEs in Canada and 459 FTEs and contract employees in Mexico. The majority of the charges were incurred during the three months ended September 29, 2019 as it related to the closure of the Dongguan manufacturing facility. During the three months ended September 29, 2019, restructuring charges of \$5.5 million were incurred related to the Dongguan facility exit, in addition to \$0.9 million incurred related to the reduction of 19 FTEs in the U.S, 4 FTEs in Canada and 89 FTEs and contract employees in Mexico. The restructuring charges related to the Dongguan facility included \$1.4 million of severance charges related to the reduction of 137 FTEs and other facility closure activities, accrued tax and duties of \$0.2 million and equipment decommissioning and facility charges of \$0.4 million. In addition, the restructuring charges included is a \$1.7 million write down of accounts receivable, a \$1.5 million write down of inventory and \$0.3 million write down of property, plant and equipment.

As at September 27, 2020, the Company had \$0.2 million of accrued restructuring charges remaining related to Dongguan to be paid by the end of the fourth quarter of 2020 mainly related to employee severance and legal fees.

Interest Expense

Interest expense decreased to \$6.0 million in the first nine months of 2020 compared to \$8.3 million in the same period in 2019. The decrease was primarily the result of the pay down of the Term Loan B Facility in addition to lower average debt balance in the first nine months of 2020 compared to the same period in 2019. The weighted average interest rates with respect to the debt on our PNC and TCW Facilities was 7.3%. The weighted average interest rates for the same period in the prior year was 10.5%.

Income Tax Expense

The Company recorded current income tax expense of \$0.9 million and \$0.6 million for the first nine months of 2020 and 2019, in connection with U.S. state taxes and taxes on profits in certain foreign jurisdictions, and deferred income tax benefit of \$15 thousand and expense of \$14 thousand in the first nine months of 2020 and 2019, in connection with temporary differences related to the Mexican operations.

Non-GAAP Financial Measures

To supplement our consolidated financial statements, which are prepared and presented in accordance with U.S. GAAP, we use the following non-GAAP financial measures: Adjusted Gross Profit, EBITDA, Adjusted EBITDA and Adjusted Net Income (collectively the "Non-GAAP Financial Measures"). We believe that these Non-GAAP Financial Measures, when used in conjunction with GAAP financial measures, provide useful information about operating results, enhance the overall understanding of past financial performance and future prospects, and allow for greater transparency with respect to the key metrics we use in our financial and operational decision making, as they exclude the effects of items that may not be indicative of, or are unrelated to, our underlying operating results, such as expenses related to the COVID-19 pandemic. The Company's management believes that adjusting for the additional temporary costs attributable to the COVID-19 pandemic allows for a better comparison of the Company's performance to prior periods, which is consistent with our recent amendments to the financial covenants in our financing agreements. These non-GAAP measures are used by the Company's management to manage and monitor the Company's performance, and also frequently used by analysts, investors and other interested parties to evaluate companies in our industry. The presentation of this financial information is not intended to be considered in isolation or as a substitute for, or superior to, the financial information prepared and presented in accordance with U.S. GAAP, and they should not be construed as an inference that our future results will be unaffected by any items adjusted for in these non-GAAP measures. In evaluating these non-GAAP measures, you should be aware that in the future we may incur expenses that are the same as or similar to some of those adjusted in this presentation. The Non-GAAP Financial Measures that we use are not necessarily comparable to similarly titled measures used by other companies due to different methods of calculation.

Net Income and Adjusted Net Income Reconciliation

Adjusted Net Income, a non-GAAP financial measure, is defined as Net Income before amortization of intangible assets, restructuring charges, stock-based compensation, fair value adjustment of warrant liability, fair value adjustment to contingent consideration, merger and acquisition related expenses and unrealized foreign exchange gains and losses on unsettled forward foreign exchange contracts and COVID-19 related expenses. Management presents Adjusted Net Income, as it is believed the information is useful to investors in understanding and evaluating our operating results as it aligns the net income (loss) with those adjustments made to EBITDA and gross profit.

Below is the reconciliation of Net Income to Adjusted Net Income (in thousands):

| | Nine months ended September 27, 2020 | Nine months ended September 29, 2019 |
|--|--|--|
| Net income (loss) | \$ 2,973 | \$ (6,991) |
| Add: | | |
| Amortization of intangible assets | 2,718 | 5,532 |
| Restructuring charges | 525 | \$ 8,624 |
| Stock based compensation | 475 | 538 |
| Fair value adjustment of warrant liability | 15 | (919) |
| Fair value adjustment of contingent consideration | — | (3,050) |
| Merger and acquisitions related expenses | — | 232 |
| COVID-19 related expenses (1) | 2,533 | — |
| Unrealized foreign exchange gain on unsettled forward foreign exchange contracts | (720) | — |
| Adjusted net income | <u>\$ 8,519</u> | <u>\$ 3,966</u> |

- (1) Includes costs attributable to the COVID-19 pandemic, including retention of temporary replacement labor, additional sanitation, cleaning and disinfection of facilities, personal protective equipment and related supplies, costs associated with facilitating social distancing and logistics costs associated with expediting inventory purchases from existing and new sources.

Net income increased to \$3.0 million from a \$7.0 million loss in the first nine months of 2020 and 2019. In addition, the increase in net income was due to a reduction in restructuring charges, increased gross profit, and unrealized foreign exchange gain on unsettled forward contracts in the third quarter of 2020 over the same period in the prior year. When excluding the items noted in the above reconciliation, Adjusted Net Income increased \$4.6 million in the first nine months of 2020 over the same period in the prior year, which is mainly due to increased gross profit, reduced interest expense due to reduction in debt and partially offset by increased selling, general and administrative expense.

Gross Profit and Adjusted Gross Profit Reconciliation

Adjusted Gross Profit, a non-GAAP financial measure, is defined as gross profit exclusive of unrealized foreign exchange gains or losses on unsettled forward foreign exchange contracts and the amortization of intangible assets. The Company calculates an adjusted gross profit amount as we consider gross profit exclusive of such unrealized foreign exchange gains or losses on unsettled forward foreign exchange contracts to be a meaningful measure as it is non-cash and management does not consider the mark-to-market valuation reflective of operating performance in the current period. Management also excludes the impact of intangible assets amortization as these charges are non-cash in nature and are not believed to be reflective of operating performance. We also believe adjusted gross profit provides useful information to investors in understanding and evaluating our operating results in the same manner as management.

Below is the reconciliation from the financial statement presentation of gross profit to the non-GAAP measure of adjusted gross profit (in thousands):

| | Nine months ended September 27, 2020 | Nine months ended September 29, 2019 |
|--|--|--|
| Gross profit | \$ 31,427 | \$ 26,527 |
| Add: | | |
| Unrealized foreign exchange gain on unsettled forward exchange contracts | (720) | — |
| Amortization of intangible assets | 2,718 | 5,532 |
| COVID-19 related expenses (1) | 2,533 | — |
| Adjusted gross profit | <u>\$ 35,958</u> | <u>\$ 32,059</u> |
| Adjusted gross profit percentage | <u>12.6 %</u> | <u>11.4 %</u> |

- (1) Includes costs attributable to the COVID-19 pandemic, including retention of temporary replacement labor, additional sanitation, cleaning and disinfection of facilities, personal protective equipment and related supplies, costs associated with facilitating social distancing and logistics costs associated with expediting inventory purchases from existing and new sources.

EBITDA and Adjusted EBITDA Reconciliation

EBITDA and Adjusted EBITDA, non-GAAP financial measures, are defined as earnings before interest, taxes, depreciation and amortization, with Adjusted EBITDA also excluding restructuring charges, stock-based compensation, unrealized foreign exchange gains and losses on unsettled forward foreign exchange contracts, fair value adjustment of warrant liability, fair value adjustment to contingent consideration and merger and acquisition related expenses and COVID-19 related expenses. Management presents EBITDA and Adjusted EBITDA, as they are utilized by management to monitor performance against budget as well as compliance with bank covenants. We also believe EBITDA and Adjusted EBITDA provide useful information to investors in understanding and evaluating our operating results in the same manner as management.

Below is the reconciliation of net income (loss), the closest GAAP measure, to EBITDA and Adjusted EBITDA (in thousands).

| | Nine months ended September 27, 2020 | Nine months ended September 29, 2019 |
|--|--|--|
| Net income (loss) | \$ 2,973 | \$ (6,991) |
| Add: | | |
| Depreciation of property, plant and equipment | 4,767 | 4,902 |
| Amortization of intangible assets | 2,718 | 5,532 |
| Interest | 6,021 | 8,349 |
| Income taxes | 857 | 606 |
| EBITDA | <u>\$ 17,336</u> | <u>\$ 12,398</u> |
| Add: | | |
| Restructuring charges | 525 | 8,624 |
| Stock based compensation | 475 | 538 |
| Fair value adjustment of warrant liability | 15 | (919) |
| Fair value adjustment to contingent consideration | — | (3,050) |
| Merger and acquisition related expenses | — | 232 |
| COVID-19 related expenses (1) | 2,533 | — |
| Unrealized foreign exchange gain on unsettled forward exchange contracts | (720) | — |
| Adjusted EBITDA | <u>\$ 20,164</u> | <u>\$ 17,823</u> |

- (1) Includes costs attributable to the COVID-19 pandemic, including retention of temporary replacement labor, additional sanitation, cleaning and disinfection of facilities, personal protective equipment and related supplies, costs associated with facilitating social distancing and logistics costs associated with expediting inventory purchases from existing and new sources.

Liquidity

As at September 27, 2020, the Company's liquidity was comprised of \$0.2 million in cash on hand and \$30.5 million of funds available to borrow under the PNC Facility, which matures on November 8, 2023. The Company funds its operations by regularly utilizing its PNC Facility (refer to Note 4). The Company manages its capital requirements through budgeting and forecasting processes while monitoring for compliance with bank covenants. Funds available under the PNC Facility are managed on a weekly basis, based on the cash flow requirements of the various operating segments. Cash flows generated from operations are immediately applied towards paying down the PNC Facility.

Market conditions, including the implications of the COVID-19 pandemic, may negatively impact our ability to secure and source alternative methods of financing. We do not currently foresee a material impact in the short term based on our working capital needs, however if a number of our customers reduce or temporarily cease payments to us, this would present a risk and negatively impact our cash flow and ability to meet our working capital obligations to operate our business, which could require us to seek alternative methods of financing.

Net cash generated from operating activities was \$2.5 million during each of the nine months ended September 27, 2020 and September 29, 2019. Working capital changes related to \$16.5 million unbilled contract asset increase, resulting in a use of cash which was due to the increase in unbilled contract assets for customers when compared to the same period in the prior year. This was partially offset by the \$12.0 million increase in the accrued liabilities due to deferred revenue for the first nine months of 2020. Accounts receivable days sales outstanding was 61 days in the first nine months of 2020 and 2019. Accounts Payable represented a source of \$3.7 million due to timing of payments. Accounts payable days outstanding increased to 72 days for the first nine months of 2020 compared to 71 days for the first nine months of 2019. Inventory turnover, on an annualized basis, decreased to 4.1 times for the first nine months of 2020 compared to 4.4 times for the first nine months of 2019.

Net cash used in financing activities during the first nine months of 2020 was \$2.4 million compared to net cash used by \$0.3 million for the first nine months of 2019. During the first nine months of 2020, the Company made net borrowing to the revolving debt of \$0.3 million, compared to the repayments to the revolving debt of \$9.9 million during the first nine months of 2019. The Company also paid down its long-term debt in the amount of \$0.9 million and 22.6 million in the first quarters of 2020 and 2019, respectively. Principal repayments on capital lease obligations were \$1.0 million in the first nine months of 2020 compared to \$1.2 million in the same period in the prior year.

Net cash used in investing activities during the first nine months of 2020 was \$1.2 million compared to \$3.2 million in the first nine months of 2019, related to capital asset purchases. During the first nine months of 2020, the Company used \$2.6 million for capital asset purchases, partially offset by leasing proceeds of \$1.4 million.

Capital Resources

The Company borrows money under the PNC Facility, which has a term ending on November 8, 2023. Advances made under the PNC Facility bear interest at the U.S. base rate plus an applicable margin ranging from 0.75% to 1.25%, or LIBOR plus an applicable margin ranging from 2.50% to 3.00%. The base commercial lending rate should approximate U.S. prime rate.

The Company also borrows money under the Financing Agreement which governs the Term A Loan Facility that matures on the Maturity Date. The Term Loan A Facility bears interest at LIBOR plus an applicable margin of 8.75% through June 30, 2020, and borrowings under the Financing Agreement will thereafter bear interest at LIBOR plus an applicable margin ranging from 7.25% to 8.75%. Payments made under the Term Loan A Facility at any time prior to the Maturity Date (other than scheduled amortization payments and mandatory prepayments) are subject to an applicable premium equal to the amount of such payment multiplied by (i) 3.00% in the event that such payment occurs before November 8, 2019, (ii) 2.00% in the event that such payment occurs after November 8, 2019, and on or before November 8, 2020, and (iii) 1.00% in the event that such payment occurs after November 8, 2020, and on or before November 8, 2021. No such applicable premium is payable for any payment of loans made under the Term Loan A Facility occurring after November 8, 2021.

The Credit Facilities are joint and several obligations of the Company and its subsidiaries that are borrowers under the facilities and are jointly and severally guaranteed by other subsidiaries of the Company. Repayment under the PNC Facility and Term A Loan Facility are collateralized by the assets of the Company and each of its subsidiaries. The Credit Facilities contain certain financial and non-financial covenants, including restrictions on dividend payments. The financial covenants under each Credit Facility require the Company to maintain a fixed charge coverage ratio and a total leverage ratio quarterly during the term of the Credit Facilities. The Company was in compliance with the financial covenants included in the Credit Facilities as at September 27, 2020.

We believe that our sources of liquidity and capital, including cash we expect to generate from operations, available cash and amounts available under our Credit Facilities, will be adequate to meet our debt service requirements, capital expenditures and working capital needs at our current level of operations for the next twelve months. However, we make no assurance that these

sources of liquidity and capital, particularly with respect to amounts available from lenders, will be sufficient to meet our future needs. We have agreed to a borrowing base formula under which the amount we are permitted to borrow under the PNC Facility is based on our accounts receivable and inventory. Further, we make 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 indebtedness will be subject to future economic conditions and to financial, business and other factors, certain of which are beyond our control.

Market conditions, including the implications of the COVID-19 pandemic, may negatively impact our ability to secure and source alternative methods of financing. We do not currently foresee a material impact in the short term based on our working capital needs, however if a number of our customers reduce or temporarily cease payments to us, this would present a risk and negatively impact our cash flow and ability to meet our working capital obligations to operate our business, which could require us to secure alternative methods of financing. In order to meet our customers' delivery requirements, we have incurred and may continue to incur COVID-19 related expenses. These are primarily due to incremental logistics costs associated with expediting inventory purchases from existing and new sources, and labor and production inefficiencies and retention of temporary replacement labor to address workplace absenteeism due to illness, potential COVID-19 exposure or personal commitments. We are currently taking steps to limit our expenses, including pausing all non-essential new hiring and new programs, and reducing our fourth quarter capital expenditures.

Item 3 Quantitative and Qualitative Disclosures about Market Risk

Interest Rate Risk

The Company borrows money under the PNC Facility, which has a term ending on November 8, 2023. Advances made under the PNC Facility bear interest at the U.S. base rate plus an applicable margin ranging from 0.75% to 1.25%, or LIBOR plus an applicable margin ranging from 2.50% to 3.00%. The base commercial lending rate should approximate U.S. prime rate.

The Company also borrows money pursuant to the Financing Agreement. The Term A Loan Facility matures on its Maturity Date. The Term Loan A Facility bears interest at LIBOR plus an applicable margin of 8.75% through June 30, 2020, and borrowings under the Financing Agreement will thereafter bear interest at LIBOR plus an applicable margin ranging from 7.25% to 8.75%. Payments made under the Term Loan A Facility at any time prior to the Maturity Date (other than scheduled amortization payments and mandatory prepayments) are subject to an applicable premium equal to the amount of such payment multiplied by (i) 3.00% in the event that such payment occurs before November 8, 2019, (ii) 2.00% in the event that such payment occurs after November 8, 2019, and on or before November 8, 2020, and (iii) 1.00% in the event that such payment occurs after November 8, 2020, and on or before November 8, 2021. No such applicable premium is payable for any payment of loans made under the Term Loan A Facility occurring after November 8, 2021.

The impact of a 10% change in interest rates would be estimated to have the following impact on our reported earnings.

| | |
|---|----------|
| 10% increase in interest rate (million) | \$ 0.5 |
| 10% decrease in interest rate (million) | \$ (0.5) |

Foreign Currency Exchange Risk

Given our global business operations, we are exposed to exchange rate fluctuations on expenditures denominated in foreign currencies. However, most of our sales and component purchases are denominated in U.S. dollars, which limits our foreign currency risk. Our foreign exchange risk relates primarily to our Canadian, Mexican and Asian payroll, Euro-based component purchases and other operating expenses denominated in local currencies in our geographic locations. To mitigate this risk, the Company enters into forward foreign exchange contracts to reduce its exposure to foreign exchange currency rate fluctuations related to forecasted Mexican peso expenditures. The strengthening of the Mexican peso would result in an increase in costs to the organization and may lead to a reduction in reported earnings.

The impact of a 10% change in exchange rates would be estimated to have the following impact on cost of sales for the Company:

| | |
|--|----------|
| 10% increase in both the CAD and PESO foreign exchange rates (million) | \$ 1.4 |
| 10% decrease in both the CAD and PESO foreign exchange rates (million) | \$ (1.7) |

Credit Risk

In the normal course of operations, there is a risk that a counterparty may default on its contractual obligations to us which would result in a financial loss that could impact our reported earnings. In order to mitigate this risk, we complete credit approval procedures for new and existing customers and obtain credit insurance where it is financially viable to do so given anticipated revenue volumes, in addition to monitoring our customers' financial performance. We believe our procedures in place to mitigate customer credit risk and the respective allowance for doubtful accounts are adequate. Although the Company takes measures to reduce credit risk, these charges can have a material impact on our financial performance.

While we continue to communicate with our customers and monitor cash collections, market conditions, including as a result of the COVID-19 pandemic, may negatively impact our customers' ability to pay. We do not currently foresee a material impact in the short term based on our customers' payment patterns, however if a number of our customers reduce or temporarily cease payments to us, this would present a risk and any charges could have a material impact on our financial performance.

There is limited risk of financial loss of defaults on our outstanding forward currency contracts as the counterparty to the transactions had a Standard and Poor's rating of A- or above as at September 27, 2020.

Liquidity Risk

There is a risk that we may not have sufficient cash available to satisfy our financial obligations as they come due. The financial liabilities we have recorded in the form of accounts payable, accrued liabilities and other current liabilities are primarily due within 90 days with the exception of the current portion of capital lease obligations which could exceed 90 days and our PNC Facility which utilizes a lock-box to pay down the obligation effectively daily. As at September 27, 2020, the Company's liquidity was comprised of \$0.2 million in cash on hand and \$30.5 million of funds available to borrow under the PNC Facility. We believe that cash flow from operations, together with cash on hand and our PNC Facility, which has a maximum credit limit of \$65.0 million of which \$30.5 million of funds were available as at September 27, 2020 is sufficient to fund our financial obligations. However, availability under the PNC Facility is subject to certain conditions, including borrowing base conditions based on eligible inventory and accounts receivable, as determined by the lender in addition to being subject to certain debt covenants.

Market conditions, including as a result of the COVID-19 pandemic, may negatively impact our ability to secure and source alternative methods of financing. We do not currently foresee a material impact in the short term based on our working capital needs, however, if a number of our customers reduce or temporarily cease payments to us, this would present a risk and negatively impact our cash flow and ability to meet our working capital obligations to operate our business, which could require us to seek alternative methods of financing, which may only be available to use on unfavorable terms, if at all.

Fair Value Measurement

The carrying values of the Company's cash, accounts receivable, accounts payable and accrued liabilities due within one-year approximate fair values due to the short-term maturity of these instruments. The Company's financial instruments at September 27, 2020, are comprised of the following:

| | As at September 27, 2020 | | As at December 29, 2019 | |
|----------------------------|--------------------------|----------------------|-------------------------|----------------------|
| | Carrying Amount | Estimated Fair Value | Carrying Amount | Estimated Fair Value |
| Level 1 | | | | |
| Cash | \$ 169 | \$ 169 | \$ 1,368 | \$ 1,368 |
| Level 2 | | | | |
| Revolving credit facility | 34,356 | 34,356 | 34,701 | 34,701 |
| Current and long term debt | 34,701 | 37,813 | 35,000 | 38,750 |
| Warrant liability | 1,746 | 1,746 | 1,730 | 1,730 |

Item 4 Controls and Procedures

Evaluation of Disclosure Controls and Procedures.

As of the end of the period covered by this quarterly report, the Company's Chief Executive Officer (Principal Executive Officer) and Chief Financial Officer (Principal Accounting Officer) have conducted an evaluation of the Company's disclosure controls and procedures as defined in Rules 13a-15(e) and 15(d)-15(e) under the Exchange Act. Based on their evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were not effective during and as at September 27, 2020 due to a material weakness in internal control over financial reporting that was disclosed in our Annual Report on Form 10-K for the fiscal year ended December 29, 2019 (the "2019 Form 10-K").

As previously described in Part II, Item 9A of our 2019 Form 10-K, we implemented a remediation plan to address the material weakness. During the nine months ended September 27, 2020, Management undertook the following actions to remediate the material weakness:

- Hired a Vice President of Information Technology and an IT SOX Consultant;
- Deployed additional training programs for IT employees;
- Performed a thorough review of the design of all IT controls with focus on those controls associated with the material weakness;
- Implemented a software platform to manage changes to in-scope systems; and
- Implemented a software platform to manage the Company's overall internal controls / SOX program.

We have commenced our testing of these controls and have not identified any deficiencies at this time. Based on these additional measures taken, the Chief Executive Officer and Chief Financial Officer have concluded that the controls that contributed to the

material weakness were remediated from a design perspective as of September 27, 2020. Based on the progress made as of September 27, 2020, we expect to confirm the remediation of this material weakness at the end of 2020. The material weakness will not be considered remediated, however, until the applicable controls operate for a sufficient period of time and management has concluded, through testing, that these controls are operating effectively. We expect that the remediation of this material weakness will be completed by the end of 2020.

Changes in Internal Control over Financial Reporting

Except for the material weakness identified during the fiscal quarter ended December 29, 2019, as of September 27, 2020, there were no changes in the Company's internal control over financial reporting that occurred during the fiscal quarter ended September 27, 2020 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Part II OTHER INFORMATION

Item 1 Legal Proceedings

None.

Item 1A Risk Factors

The following additional risk factor should be read in conjunction with the risk factors previously disclosed in Part I, Item 1A, "Risk Factors," of our Form 10-K for the fiscal year ended December 29, 2019 ("Annual Report") and our other reports and registration statements filed with the SEC. The developments described in this additional risk factor have heightened, or in some cases manifested, certain of the risks disclosed in the risk factor section of our Annual Report, and such risk factors are further qualified by the information relating to the COVID-19 pandemic that is described in this Quarterly Report on Form 10-Q, including in the additional risk factor below. Except as described herein, there have been no material changes in our risk factors disclosed in our Annual Report.

The effect of COVID-19 on our operations and the operations of our customers, suppliers and logistics providers has, and is expected to continue to have a material, adverse impact on our financial condition and results of operations.

Our global operations expose us to risk arising from the global COVID-19 pandemic, which has had and will continue to have an adverse impact on our employees, operations, supply chain and distribution system. While we have taken numerous steps to mitigate the impact of the pandemic on our results of operations, we make no assurance that these efforts will be successful. To date, COVID-19 has increased our expenses, primarily related to additional temporary labor costs, additional sanitation, cleaning and disinfection of facilities, procurement of personal protection equipment and related supplies, costs associated with facilitating social distancing and logistics costs associated with expediting inventory purchases for new and existing sources. COVID-19 has spread across the globe and is impacting worldwide economic activity, including our international manufacturing facilities. Public and private sector policies and initiatives to reduce the transmission of COVID-19, including travel restrictions and quarantines, are impacting our operations, including affecting the ability of our employees to get to our facilities, reducing capacity utilization levels, and interrupting the movement or increasing the cost of moving components and products through our supply chain. If we are required to close our facilities or further reductions in capacity utilization occur, we may incur additional direct costs and lose revenue. If our suppliers experience additional closures or reductions in their capacity utilization levels in the future, we may have difficulty sourcing materials necessary to fulfill production requirements. The COVID-19 pandemic has also impacted our customers and may create unpredictable reductions or increases in demand for our manufacturing services. Our ability to continue to manufacture products is highly dependent on maintaining the safety and health of our employees. The ability of our employees to work may be significantly impacted by individuals contracting or being exposed to COVID-19. While we are following the requirements of governmental authorities and taking preventative and protective measures to prioritize the safety of our employees, these measures may not be successful, and we may be required to temporarily close facilities or take other measures. In addition, responding to the continuing pandemic could divert management's attention from our key strategic priorities, cause us to reduce, delay, alter or abandon initiatives that may otherwise increase our long-term value or otherwise disrupt our business operations. While we are staying in close communication with our sites, employees, customers, suppliers and logistics partners and acting to mitigate the impact of this dynamic and evolving situation, the duration and extent of these impacts on us is not determinable. We believe the COVID-19 pandemic could have a material and adverse material impact on our consolidated financial position, results of operations and cash flows in the future. In addition, the impact of the COVID-19 pandemic may exacerbate other risks we face. Due to these possible impacts of the COVID-19 pandemic and as generally described in this quarterly report, the Company's consolidated financial position, results of operations and cash flows for the first nine months of 2020 are not necessarily indicative of future performance.

Item 2 Unregistered Sales of Equity Securities and Use of Proceeds

None.

Item 3 Defaults Upon Senior Securities

None.

Item 4 Mine Safety Disclosures

Not applicable.

Item 5 Other Information

None.

Item 6 Exhibits

EXHIBIT INDEX

| | |
|----------|---|
| 10.1 | <u>Fifth Amendment to Amended and Restated Revolving Credit and Security Agreement, by and among SMTC Corporation, SMTC Manufacturing Corporation of California, SMTC Mex Holdings, Inc., HTM Holdings, Inc., MC Test Service, Inc., MC Assembly International LLC, MC Assembly LLC, the financial institutions party thereto and PNC Bank, National Association, as agent for the lenders, dated September 25, 2020 (1).</u> |
| 10.2 | <u>Amendment No. 6 to Financing Agreement, by and among SMTC Corporation, the borrowers party thereto, each other loan party thereto, the lenders party thereto, TCW Asset Management Company LLC, as administrative agent for the lenders, and TCW Asset Management Company LLC, as collateral agent for the lenders, dated September 25, 2020 (2).</u> |
| 31.1* | <u>Certification of Edward Smith pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated November 5, 2020.</u> |
| 31.2* | <u>Certification of Steve Waszak pursuant to Section 302 of the Sarbanes-Oxley Act of 2002, dated November 5, 2020.</u> |
| 32.1* | <u>Certification of Edward Smith, 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 5, 2020.</u> |
| 32.2* | <u>Certification of Steve Waszak, 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 5, 2020.</u> |
| 101.INS* | Inline XBRL Instance Document – the instance document does not appear in the Interactive Data File because XBRL tags are embedded within the Inline XBRL document. |
| 101.SCH* | Inline XBRL Taxonomy Extension Schema Document |
| 101.CAL* | Inline XBRL Taxonomy Extension Calculation Linkbase Document |
| 101.DEF* | Inline XBRL Taxonomy Extension Definition Linkbase Document |
| 101.LAB* | Inline XBRL Taxonomy Extension Label Linkbase Document |
| 101.LAB* | Inline XBRL Taxonomy Extension Presentation Linkbase Document |
| 104 | Cover Page Interactive Data File (embedded within the Inline XBRL document) |

* Filed herewith

- (1) Filed as Exhibit 10.1 to the registrant's Current Report on Form 8-K filed on September 28, 2020 (File No. 000-31051) and incorporated by reference herein.
- (2) Filed as Exhibit 10.2 to the registrant's Current Report on Form 8-K filed on September 28, 2020 (File No. 000-31051) and incorporated by reference herein.

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/ Edward Smith

Name: Edward Smith

Title: President and Chief Executive Officer

By: /s/ Steve Waszak

Name: Steve Waszak

Title: Chief Financial Officer (Principal Accounting Officer)

Date: November 5, 2020

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

CERTIFICATION

I, Edward Smith, 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles of the United States of America;
 - (c) 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
 - (d) 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 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 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 5, 2020

By: /s/ Edward Smith
Edward Smith
President and Chief Executive Officer

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

CERTIFICATION

I, Steve Waszak, 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)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) 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) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles of the United States of America;
 - (c) 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
 - (d) 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 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 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 5, 2020

By: /s/ Steve Waszak
Steve Waszak
Chief 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 27, 2020 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 27, 2020 fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Edward Smith

Edward Smith
President and Chief Executive Officer

Date: November 5, 2020

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 27, 2020 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 27, 2020 fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Steve Waszak

Steve Waszak
Chief Financial Officer

Date: November 5, 2020

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.