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PLXS - Q4 2013 Plexus Earnings Conference Call

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OVERVIEW:

Co. reported 4Q13 revenue of \$568m and diluted EPS of \$0.71. Expects 1Q14 revenue to be \$520-550m and diluted EPS, excluding any restructuring charges and including \$0.08 of stock based compensation expense suggesting solid operating performance, to be \$0.57-0.63.



CORPORATE PARTICIPANTS

Angelo Ninivaggi *Plexus Corporation - SVP, Chief Administrative Officer, General Counsel, Secretary*

Dean Foate *Plexus Corporation - President, CEO*

Todd Kelsey *Plexus Corporation - EVP, COO*

Ginger Jones *Plexus Corporation - SVP, CFO*

CONFERENCE CALL PARTICIPANTS

Jim Suva *Citi - Analyst*

Sherri Scribner *Deutsche Bank - Analyst*

Shawn Harrison *Longbow Research - Analyst*

Brian Alexander *Raymond James - Analyst*

Amit Daryanani *RBC Capital Markets - Analyst*

Steven Fox *Cross Research - Analyst*

Mark Delaney *Goldman Sachs - Analyst*

Sean Hannan *Needham & Company - Analyst*

PRESENTATION

Operator

Good morning, ladies and gentlemen, and welcome to the Plexus Corporation conference call regarding its fiscal fourth quarter 2013 earnings announcement. My name is Dawn and I will be the operator for today's call. At this time, all participants are in a listen-only mode. After a brief discussion by management, we will open the conference call for questions. The conference call is scheduled to last approximately one hour. Please note that this conference is being recorded.

I will now turn the call over to Mr. Angelo Ninivaggi, Plexus Senior Vice President, Chief Administrative Officer, General Counsel and Secretary. Mr. Ninivaggi, please go ahead.

Angelo Ninivaggi - *Plexus Corporation - SVP, Chief Administrative Officer, General Counsel, Secretary*

Good morning and thank you all for joining us today. Before we begin, I should remind everyone that statements made during our call today that are not historical in nature, such as statements in the future tense and statements that include believe, expect, intend, plan, anticipate and similar terms and concepts, are forward-looking statements.

Forward-looking statements are not guarantees since there are inherent difficulties in predicting future results and actual results could differ materially from those expressed or implied in the forward-looking statements. For a list of major factors that could cause actual results to differ materially from those projected, please refer to the Company's periodic SEC filings, particularly the risk factors in our Form 10-K for the fiscal year ended September 29, 2012 and the safe harbor and fair disclosure statement in yesterday's press release.

The Company provides non-GAAP supplemental information. For example, our call today will reference return on invested capital and free cash flow. These are non-GAAP financial measures and they are used for internal management assessments because they provide additional insight into ongoing financial performance and the metrics that are driving management decisions. For a full reconciliation of non-GAAP supplemental information, please refer to yesterday's press release and our periodic SEC filings.

We encourage participants on this call this morning to access the live webcast and supporting materials on the Plexus website at www.plexus.com by clicking on Investor Relations at the top of the page and then Event Calendar.

Joining me this morning are Dean Foate, Chairman, President and Chief Executive Officer; Ginger Jones, Senior Vice President and Chief Financial Officer; and Todd Kelsey, Executive Vice President and Chief Operating Officer. Let me now turn the call over to Dean Foate. Dean?

Dean Foate - Plexus Corporation - President, CEO

Thank you, Angelo, and good morning, everyone. For those following along on the website material, please advance to slide three.

Last night, we reported results for our fiscal fourth quarter of 2013. Revenues were \$568 million, above the midpoint of our guidance range, but modestly down from the prior quarter. Diluted EPS of \$0.71 was above the higher end of our revised EPS guidance range that we increased leading into our Investor Day in early September.

While our EPS result benefited from discrete tax items, the underlying result was still strong as a consequence of improved operating performance.

Before Todd and then Ginger get into the details on the quarter, I will provide a brief wrap up of fiscal 2013 and then I will share some thoughts on fiscal 2014 that give us cause for optimism. Please advance to slide four.

First, results versus goals. There's no way to sugar coat the results. Fiscal 2013 was certainly not the year we anticipated. Back in August of 2012, looking into fiscal 2013, we had a revenue plan that indicated a path to mid-teens growth. As the first half of the year unfolded, we experienced broad-based reductions in customer forecasts, as it became evident to many of our customers that end market growth would be challenging. Further, in our fiscal first quarter of 2012, we were notified by our largest customer that they would disengage by the end of our fiscal year.

We finished fiscal 2013 with revenue down 3.4%. Despite the revenue decline, we managed to keep our return on invested capital performance in value-creation territory with a result of 14% or 200 basis points of overweighted average cost of capital.

Slide five. Our secular performance relative to the prior year provides insight into how we arrived at the final result for the year. Our Networking/Communications sector was down approximately 9% from the prior year. When compared to our original plan for the year, our Networking/Communications sector accounted for more than 70% of our forecast decline. Clearly, our Networking/Communications customers face significant challenges in their end markets.

Our Healthcare/Life Sciences sector performed reasonably well this year, up 14% over the prior year, driven by a combination of share gains and new customer engagements. I believe our team did a nice job growing this sector in the face of a challenging macro.

Our Industrial/Commercial sector was down 18% for the year. Our full-year plan anticipated a revenue contraction for this sector, as a significant customer substantially reduced their forecast to adjust inventory levels. That reduction, in combination with other end market challenges, led to a deeper contraction than originally anticipated. While we certainly had some solid business wins in our Industrial/Commercial sector, the new business ramps did not overcome the broader economic weakness and specific customer challenges.

Our Defense/Security/Aerospace sector performed well, with revenues up 21% and in line with our full-year plan. The strength was largely driven by aerospace component of the sector, as our team did a nice job gaining share with customers and engaging new customers to drive future growth.

In summary, we had a mixed year in terms of our sector performance. The positive news is that we gained share in sectors that have longer product life cycles, place greater value on our Engineering Solutions business, require greater regulatory compliance, and as a consequence, are generally stickier, enduring relationships.

Additionally, we exited the year with lower customer concentration risk and a healthier portfolio mix across our sectors. Looking ahead to fiscal 2014, we currently anticipate solid growth in all our sectors except Networking/Communications, where we are unlikely to overcome the full \$284 million headwind associated with the Juniper disengagement.

Turning now to a few fiscal 2013 highlights on slide six. Despite the revenue challenges, our team did a nice job driving quarter-over-quarter improvement in operating profit throughout the year. Our focus on supply chain, productivity and cost management initiatives was evident in the results.

Our working capital management initiative delivered a 10-day improvement in our cash cycle and we generated over \$100 million in free cash flow. Returning some of that cash to shareholders was our \$50 million share buyback program.

By improving our operating performance, we invested in new facilities in the EMEA region to enhance our value proposition in that important growth market. In the Americas, we constructed a new facility in the Fox Cities, Wisconsin to enable consolidation of three existing facilities during the first half of fiscal 2014, leading to lower operating costs in this state-of-the-art facility.

Additionally, in fiscal quarter four, we announced our intent to lease a facility that's currently under construction in Guadalajara, Mexico.

Finally, our team did an outstanding job managing professionally through the challenges of the Juniper disengagement, with no surprises for Plexus or for Juniper.

Slide seven. While fiscal 2013 was a challenging year, much of our effort positions Plexus for a better fiscal 2014, providing cause for optimism. Our sector mix is certainly healthier and customer concentration risk lower. Our teams did a nice job gaining share with customers and adding important new growth accounts to our customer portfolio, leading us to anticipate quarter-over-quarter growth throughout the year.

We have completed a number of strategic investments that lead us to lower planned capital spending levels on facility projects over the next few years. We will continue to invest in value-stream solutions that have relatively lower invested capital and higher margins, such as our Engineering Solutions business, sustaining solutions and microelectronics.

Finally, our initiatives have created a solid path that get us back to 5% operating profit as we exit fiscal 2014. With the achievement of our financial model, we should deliver improved economic profit for the year.

Now for our guidance on slide eight. We are establishing fiscal first-quarter 2014 revenue guidance of \$520 million to \$550 million. The midpoint of this guidance range suggests that our fiscal first-quarter revenue will be down 6% when compared to our fiscal fourth quarter. The Juniper revenue headwind in fiscal Q1 is about \$42 million. So backing out Juniper, the remainder of our business should grow about 2% at the guidance midpoint.

Our diluted EPS guidance is in the range of \$0.57 to \$0.63, excluding any restructuring charges and including \$0.08 of stock-based compensation expense, suggesting solid operating performance.

I will now turn the call over to Todd Kelsey, our Chief Operating Officer.

Todd Kelsey - Plexus Corporation - EVP, COO

Thank you, Dean. Good morning. Advancing now to slide nine for some insight into the performance of our market sectors during our fiscal fourth quarter of 2013 and our current expectations for Q1 of fiscal 2014.

Our Networking/Communications sector was down about 10% sequentially in fiscal Q4. The result was slightly better than our expectations for a low- to mid-teens percentage decline as four of our top 10 customers in this sector significantly outperformed earlier forecasts.



Excluding Juniper, fiscal Q4 Networking/Communications revenues were up 17% sequentially as a result of the growth of our top customers and new program ramps. As anticipated, Juniper revenue finished at \$42 million, down \$43 million from Q3 F13. We completed all Juniper inventory shipments in fiscal Q4 and have successfully mitigated all risk involved in the disengagement. We are cautiously guiding a high teens percentage decline in our Networking/Communications sector revenues in fiscal Q1, as we feel the full impact of the Juniper disengagement.

While we are still seeing volatility in end markets, there are signs of modest strengthening from earlier forecast periods, particularly in wireless infrastructure. We are benefiting from customers that are ramping new programs or forecasting improved end market demand. Excluding Juniper revenues, we are projecting low-single-digit growth within this sector during Q1.

Our Healthcare/Life Sciences sector performed above our original expectations, with the revenue result up about 12% sequentially, as most of our top customers performed above expectations. We originally expected high-single-digit growth.

Looking ahead to fiscal Q1, we currently anticipate revenues in our Healthcare/Life Sciences sector to be flat to Q4. In future quarters, we are seeing increased growth as a result of new program ramps.

Our Industrial/Commercial sector was up sequentially about 4% in our fiscal Q4. This was in line with our expectations of mid-single-digit growth, despite the fact that two of our top customers fell short of earlier forecasts. We currently anticipate that our Industrial/Commercial sector will be down in the mid-single-digit percentage range in our fiscal Q1 as we are seeing softening with several key customers.

Our Defense/Security/Aerospace sector was down about 6% in Q4, a result that was softer than our expectations of flat to the previous quarter. Several of our top customers missed expectations, dominated by a major security customer. The aerospace component of this sector was mixed.

We currently expect Q1 to be up in the high-single-digit percentage range to Q4 as we see strengthening in aerospace due to new program ramps, partially offset by further softening due to seasonality with a major security customer.

Turning now to new business wins on slide 10. During the quarter, won 34 new programs in our Manufacturing Solutions group that we anticipate will generate approximately \$155 million in annualized revenue when fully ramped into production, a result in line with our goal. The new program wins performance was nicely balanced across our regions, with APAC the largest at 40% of the win revenue.

On a sector basis, our Healthcare/Life Sciences sector had an exceptional quarter with \$83 million in wins. We continue to leverage our quality, regulatory and engineering solutions expertise within this critical market sector to drive increased market share. These Healthcare/Life Sciences wins were dominated by new programs from existing customers within the sector.

In addition, we had another strong quarter in Engineering Solutions, with new program wins totaling approximately \$19 million. Our Engineering wins were particularly strong in our Healthcare/Life Sciences sector, where we continue to differentiate marketplace.

Slide 11. Our wins performance in fiscal Q4, as shown by the overlay green bars, was down from our very strong Q3 and was above our goal. Our trailing four quarters wins, as shown by the blue bar, finished F13 at \$703 million, which is sufficient to keep our wins momentum well above our 25% goal. This key metric is currently 32%, which we believe is a very healthy number. We are driving hard to continue this performance in coming quarters to sustain our goal of returning to growth in fiscal 2014.

Advancing to slide 12. Our funnel of new opportunities remains strong at \$2 billion, slightly below the previous quarter. Our objective is to continue to harvest at the rate we achieved in fiscal 2013 while backfilling the funnel. We believe a total funnel of \$2 billion is sufficient to sustain our wins performance.

As we enter fiscal 2014, we have started to transition into our new facility in Wisconsin. As we announced in May 2012, we are pursuing a consolidation strategy of facilities in Wisconsin. We constructed a new 418,000-square-foot manufacturing facility, which is shown on slide 13. This site enables us to exit two leased facilities in Neenah, Wisconsin and one smaller owned facility in Appleton, Wisconsin. The efficiencies from the transitions enable us to deliver improvements to gross margin when the consolidation is completed.



We have finished relocating our Healthcare/Life Sciences programs into the new facility. This portion of the consolidation was completed flawlessly. The remainder of the Neenah transition will occur over the first half of fiscal 2014, and we expect to incur restructuring charges of approximately \$3 million to \$4 million in severance, facility exit costs and costs to move equipment. This estimated total is down from what we provided last quarter.

We also broke ground on our new leased facility in Guadalajara, Mexico. This will be a 265,000-square-foot facility to enable further penetration into the low-cost Americas market. Construction is expected to be complete in the third fiscal quarter of 2014.

Now we will turn to our recent cash cycle performance on slide 14. Our net cash cycle days for Q4 ended at 53 days, a low mark for the past several years. Our cash cycle was positively impacted by the timing of Juniper inventory sales, as well as strong inventory management.

When viewing our midterm trend, our days of inventory and our net cash cycle base have reduced by more than 20 days over the past three fiscal years, significantly contributing to our free cash flow. This performance was accomplished through new tools and processes facilitated by strong organizational collaboration.

While near-term we expect slightly increased cash cycle days, we have initiatives in place to maintain a net cash cycle near or under 60 days.

Finally, as shown on slide 15, I would like to highlight the progress of certain operational initiatives discussed at Investor Day last month. Our supply chain team and Manufacturing Solutions organization has made strong progress in productivity initiatives. As a result, we were able to expand operating margins from 4% to 4.7% over the course of the fiscal year. This includes an increase from 4.4% in Q3 to 4.7% in Q4 despite a slight contraction of revenue. These efforts will continue throughout fiscal 2014, where we will also benefit from the facilities consolidations in Neenah, enabling our expectation of exiting the fiscal year at our financial model.

We are making substantial progress on longer-term operational initiatives as well. I would like to highlight progress in microelectronics. We have put in place a general manager and a dedicated subject matter expert focused on new business development. We also started construction of a new clean room at our Boise Center of Excellence which triples our square footage and houses upgraded equipment. These investments have directly contributed to two recent wins totaling over \$20 million in annualized revenue when fully ramped and a substantially improved funnel. As a reminder, Micro E operating margins are significantly higher than base manufacturing.

Our operating performance initiatives underway are designed to return us to our targeted operating margin goal of 5% as we exit F14 and maintain this performance over the long-term. While we expect a pause in our progress this quarter and seasonal challenges in Q2, our efforts related to our footprint and with operational initiatives provides confidence that we have a better operating platform to service our customers and improved operating performance necessary to reach our financial goals.

With that, I will turn the call to Ginger for a more detailed review of our financial performance. Ginger?

Ginger Jones - Plexus Corporation - SVP, CFO

Thank you, Todd. Our fiscal fourth-quarter results are summarized on slide 16. Fourth-quarter revenue was \$568 million, above the midpoint of the guidance range for the quarter. Gross margin was 9.6% for the fiscal fourth quarter, below our expectations and slightly below our fiscal third-quarter results of 9.7%. Gross margin included charges of approximately \$0.4 million related to the consolidation of manufacturing facilities in Neenah, Wisconsin, which are reported as part of our ongoing results.

Selling and administrative expenses were \$28 million, below our expectations for the quarter as a result of focused cost management. SG&A as a percentage of revenue was 4.9% in the fiscal fourth quarter, lower than the fiscal third quarter. As a result, operating margin was above our expectations at 4.7%.

We recorded a tax benefit of \$42,000 during the fiscal fourth quarter, the net result of \$1.5 million of discrete tax benefit recorded during the quarter. The discrete tax items related primarily to nonrecurring adjustments in certain deferred tax assets and liabilities, offset by a valuation



allowance established against the Company's net deferred tax assets in the United Kingdom. This resulted in lower tax expense and positively impacted diluted EPS by \$0.04.

Turning now to the balance sheet on slide 17. Return on invested capital was 14% for the fiscal fourth quarter of 2013, an 80 basis point improvement from the prior quarter and 200 basis points above our weighted average cost of capital for fiscal 2013 of 12%.

During the quarter, we repurchased 411,000 of our shares for approximately \$13.8 million at a weighted average price of \$33.60 per share. Fiscal year to date, we've purchased 49.9 million of our shares under this program at an average price of \$27.37 per share.

The Plexus Board of Directors authorized a \$30 million stock repurchase program for fiscal 2014, to be funded with existing cash. The Company expects to complete the new authorized repurchases on a relatively consistent basis over fiscal 2014.

Our cash cycle for the fiscal fourth quarter was 53 days, lower than our expectations and six days lower than our results in the fiscal third quarter. This is another very good result for us, as Todd has discussed, a reflection of the working capital initiatives we've been working on for several years and the impact of the Juniper disengagement. In total, working capital decreased by approximately \$38 million during the quarter.

Free cash flow during the quarter was very strong at \$68 million. During the quarter, we generated \$92 million in cash from operations and spent \$24 million in capital expenditures, with approximately \$9 million of that capital for footprint expansion in Wisconsin and Mexico.

Dean already provided revenue and EPS guidance. I will now turn to some additional comments on the fiscal first quarter of 2014, which are summarized on slide 18.

We expect restructuring costs of \$1.5 million to \$2 million in the fiscal first quarter related to the consolidation of three facilities into our new Neenah manufacturing facility. These costs are excluded from the guidance discussed today.

Gross margin is expected to be in the range of 9.6% to 9.8%, better than our gross margin of 9.6% in the fiscal fourth quarter of 2013. We will be able to improve margins from the prior quarter despite the lower revenue as a result of the concerted efforts to improve margins that Todd covered earlier.

We expect SG&A costs to be lower than spending in the fiscal fourth quarter, in the range of \$26 million to \$27 million. At the midpoint of our guidance range for revenue, this will result in approximately 4.9% to 5% SG&A as a percentage of revenue. This improvement from the prior quarter is the result of our continued focused cost management.

This results in expected operating margin of approximately 4.6% to 4.8%, which demonstrates our commitment to returning to our targeted operating margin of 5% as we exit fiscal 2014.

A few other notes. Depreciation and amortization expense is expected to be approximately \$12 million in the fiscal first quarter, down slightly from the \$12.2 million in the fiscal fourth quarter.

We are estimating a tax rate for fiscal 2014 of 8% to 10%, above our fiscal 2012 tax rate of 3.2%.

Our expectations for the balance sheet are for working capital dollars to be up from the fiscal fourth quarter. Based on the forecasted levels of revenue, we expect these changes will result in cash cycle days, net of cash deposits, of 60 to 64 days for the fiscal first quarter of 2014. This increase in days includes increased working capital dollars to support the expected higher levels of revenue in the fiscal second quarter.

Our capital spending forecast for 2014 is approximately \$75 million. The majority of this estimate is equipment spending and the leasehold improvements for our new leased facility in Guadalajara, Mexico.

With that, we will open the call for questions. We ask that you please limit yourself to one question and one follow-up. Operator?

QUESTIONS AND ANSWERS

Operator

(Operator Instructions). Jim Suva, Citi.

Jim Suva - Citi - Analyst

Thank you very much and good morning to you and your team there. Dean and Ginger, when we look at your funnel of the new wins that you just recently have, and I think it was \$155 million for the quarter, definitely it's strong and above your long-term goal to sustain the revenue growth that you envision.

The question I have though is it is down year-over-year and quarter-over-quarter. I am wondering is there anything related in there related to the federal government spending over the past few quarters that had some extra upside to it. Or I'm just kind of wondering, are you conscious that it is down quarter-over-quarter and year-over-year, and is it something to be concerned and conscious of, or is there anything in there that we just need to be mindful of?

Dean Foate - Plexus Corporation - President, CEO

Yes, I don't know that we could look at the funnel and specifically suggest that the funnel itself, the \$2 billion funnel, that the government shutdown or anything had any specific impact on it.

We know that it had a little bit of impact on certain customers in terms of forecasting demand, which would have had more impact on our revenue forecast, our revenue picture near-term.

In terms of the overall trend, I mean, Todd is free to comment on this, but this is a lot of these things, where it's down a little bit from the prior quarter and maybe where it has been, but part of that is because we've been harvesting business out of it. I think that my point is that there's lots of things to worry about. I worry about things that I tend to not be able to control -- the economic, the lack of economic acceleration in the US and Europe, those are things to worry about. Where healthcare costs are going in the US, that's something to worry about.

Do I think that building the funnel up and getting it a little stronger and making sure we keep that win rate up is a thing to worry about? No, because I think we can control that, and I think it's certainly something we need to focus on, though.

Jim Suva - Citi - Analyst

Okay. And then I was also referring to the new business wins of \$155 million, of those both also being down.

Dean Foate - Plexus Corporation - President, CEO

Yes, I will let Todd comment on that, and we'll see where that goes. But I have a thought on that as well. So go ahead, Todd.

Todd Kelsey - Plexus Corporation - EVP, COO

So Jim, certainly we look at the magnitude of the number, but we feel good about the magnitude, the \$155 million. And one of the things, if you think back to Investor Day, we talked about really being more selective in Networking/Communications. I think you are seeing some of the impact there.



While we really don't separate wins or we count the wins number as a single number, the reality is call -- it the duration or the impact of the wins on our revenue varies significantly between the sectors.

So the Networking/Communications wins is down from what it had been previously. That tends to be more volatile revenue that needs to be replenished at a more rapid rate. If you look at -- and I did highlight our Healthcare/Life Sciences wins at \$83 million. That tends to be long-term, enduring revenue.

So I think when you look at the breakdown in the sectors that the wins are coming in, we feel really good about the wins number.

The same holds true with the funnel. Our Networking/Comms final is about half the size of our other sectors as we become more selective in that space.

Dean Foate - Plexus Corporation - President, CEO

At the risk of overanswering the question, I'm going to do it anyway. Like Todd said, we often talk about the replacement business that we have, if we stood still, what's the number of products or the amount of revenue that goes into Life or comes down related to cost-downs. And we tend to talk about that as a single number for the whole Company.

Now the reality is -- which is where Todd was going -- is if you think about Defense/Security/Aerospace, the product lifecycles in aerospace, for instance, or defense can be as much as 20 years. And so when you win a program, even though it's a modest program, it lasts a long time and so subsequent wins, of course, stack on top of that base of business.

On the other end of the spectrum, the product life cycles in Network/Communications are very short, and can be as short as 1.5 years or maybe as long as three years. And so the amount of business you have to replace in that sector is substantial in order to stay even.

So I think when you look at the balance of the wins, a lot of it is tilted in the current quarter obviously toward healthcare. These are programs that have, again, kind of in the middle range of product life cycles and will have more enduring revenue in the overall revenue picture.

So I think we are in pretty good shape at that \$155 million, which I will remind everybody is still well above where we need to be in order to sustain our 12% longer-term target for growth.

Jim Suva - Citi - Analyst

Great, thank you for the detail.

Operator

Sherri Scribner, Deutsche Bank.

Sherri Scribner - Deutsche Bank - Analyst

Ginger, I was hoping you could give us a little bit of long-term detail on the SG&A. You guys did a great job on SG&A this quarter, and the guidance suggests that SG&A is down again in December. When do you expect that to plateau and at what point would you expect that to start to tick up again?

Ginger Jones - Plexus Corporation - SVP, CFO

Thanks, Sherry. As we've talked about before, we generally have an uptick in our SG&A spending in our fiscal second quarter, which is the March quarter. So I would expect SG&A to come up about \$1 million in March and then stay relatively consistent through the end of the fiscal year at about \$28 million.

So we have done some nice job managing our SG&A cost and we will see the benefit of that. In the first quarter, it will tick up a bit in March, but still stay at a very manageable rate through the end of the fiscal year at close to \$28 million.

Sherri Scribner - Deutsche Bank - Analyst

Okay. And then in terms of the cost savings and the actions you've taken, would you say that those are relatively done and you've worked through those, or is there more to come and where would we see that benefit? Thanks.

Ginger Jones - Plexus Corporation - SVP, CFO

I think we have done most of that work. And as you know, we have had some changes in our revenues structure so we are trying to make sure that we are removing costs where we can, and I think we've done a good job of that. I think we fully reflected that in the Q1 forecast. I don't know that it gets much lower than that. And I think if we can sustain at that \$28 million level through quarters two, three, four, that gets to a good result for the fiscal year, and that is our -- we would consider that a success.

Sherri Scribner - Deutsche Bank - Analyst

Thank you.

Operator

Shawn Harrison, Longbow Research.

Shawn Harrison - Longbow Research - Analyst

Just a quick clarification first. Dean, could you remind me what the minimum amount of program wins you need to see right now to hit that 12% growth?

And then my actual question is more based upon the comment that you expect to see sequential growth throughout the year. If I am reading the tea leaves right, your view on the macro is still pretty dim and so all that would be coming from continued new program contributions.

Dean Foate - Plexus Corporation - President, CEO

I'm going to let Todd take the wins number.

Todd Kelsey - Plexus Corporation - EVP, COO

So the wins number that we are shooting for is 25% of revenue, in essence, so it would be a little bit under \$150 million; sitting about \$140 million at this point, if you did the math on it.

Dean Foate - Plexus Corporation - President, CEO

Relative to the full-year sequential growth, obviously, the sequential growth, we are not expecting the macro in our forecast. And frankly, when I look at our customers' forecast this time this year versus this time last year, clearly they are not betting on an acceleration in the macro either.

So the sequential growth that we expect to see quarter over quarter is going to be largely driven from programs that were won throughout fiscal 2013 and programs we will win in fiscal 2014 or expect to win. Aside from a couple of individual customers that have some new product technologies that are doing well and growing organically, and aside from where I will say the strength is in aerospace, aerospace continues to be a strong end market.

Shawn Harrison - Longbow Research - Analyst

Okay, and on those ramps, have you seen any -- there was, I think, talk over the past two quarters of maybe a little bit of a pushout in some of the ramps. Has that extended any further or are you kind of still seeing the same rate of program ramps as you were 90 days ago?

Todd Kelsey - Plexus Corporation - EVP, COO

This is Todd. I would say we are seeing a pretty similar situation. I think the ramps are all progressing, perhaps a little bit more muted overall is the way we'd look at it.

Shawn Harrison - Longbow Research - Analyst

Okay, that's helpful, Todd. Thanks so much.

Operator

Brian Alexander, Raymond James.

Brian Alexander - Raymond James - Analyst

Ginger, sorry if I missed this earlier, but the gross margin coming in a little bit below your guidance in September, was that Juniper-related or maybe just some more color there?

And just your overall confidence in building off the December operating margin of 4.7%. I thought Todd alluded to some seasonality challenges in the fiscal second quarter related to margin, yet you talked about building working capital in December to support higher revenue in March. So I am just confused about those two statements.

Todd Kelsey - Plexus Corporation - EVP, COO

Brian, this is Todd. I will take the gross margin question. So I think first of all, it's important to note that we don't have a gross margin target. So while we talk about it, we are really focused on the bottom line and really driving back to the 5% operating profit margin goal.

But there are two factors that really came into play with gross margins, and the first one was the expenses that we incurred as a result of the Wisconsin consolidation. So these occurred -- incurred in Q4 and amounted to about \$400,000.



The second is really around our operating initiatives that we have in play. And we really had a focus in particular over the last quarter in driving more resources to where the action is. So it really -- that involves adding resources at sites and regions and really taking it out of the corporate structure. So it's really focused on investing in our initiatives that we have in play.

Ginger Jones - Plexus Corporation - SVP, CFO

I will take the second part of that question, which is around the operating margin for the full year. You are correct; we do expect a seasonal decline in operating margin in our fiscal Q2, although our current forecast suggests that revenue will be up, so that will certainly help operating margins.

The downside of that is we do have structural costs in the March quarter that every year we tend to have a different operating margin. And that comes from salary increases that we give to our employees around the world and resetting of US payroll tax, which happens in the March quarter. So we generally see some downward pressure on margins from that in the second quarter.

So our current view is that revenue will increase sequentially throughout the year. We will see a dip in operating margin in the second quarter from those structural costs, and then increase through the balance of the year as we focus on hitting the 5% operating margin as we exit the year.

Brian Alexander - Raymond James - Analyst

Great, that's helpful. And then just a follow-up on cash flow. Any change in your cash flow outlook in 2014, I think versus what you gave at the Analyst Day, given that your working capital for the September quarter came in a lot lower than you thought it would, and I think you talked about seeing a pickup in December? So I'm not sure that changes your overall cash flow outlook for fiscal 2014.

Ginger Jones - Plexus Corporation - SVP, CFO

It does not at this point, and I think we are still working through what the working capital needs will be throughout fiscal 2014. We had this unusual impact of the Juniper exit in Q4. We hope to sustain working capital days around the 60-day level, and I think based on that, we would have a good free cash flow year, in the \$50 million to \$60 million range, but probably not as high as we had this year.

Brian Alexander - Raymond James - Analyst

Okay, thank you.

Operator

Amit Daryanani, RBC Capital Markets.

Amit Daryanani - RBC Capital Markets - Analyst

Thanks a lot. Good morning, guys. I'm sorry if I missed this, but my math would suggest Juniper business is about \$40 million revenues in the December quarter guide. Is that an accurate number? If you could confirm that.

And if it is, I guess my question really is if I adjust for Juniper, X Juniper, I guess, year-over-year you guys only grew 6%, 6.5% in Q1. Maybe you could talk about how do you achieve that 12% growth bogey for the full year given at least Q1 is going to be well below that, X Juniper.



Ginger Jones - Plexus Corporation - SVP, CFO

So we had \$42 million of Juniper revenue in the September quarter and then we are done. So the headwind as we go into December is a \$42 million headwind for Juniper. Was that your question?

Amit Daryanani - RBC Capital Markets - Analyst

Yes, yes. All right, fair enough.

Dean Foate - Plexus Corporation - President, CEO

So the math in this says that the rest of the business grows about 2% quarter to quarter, Q4 to our fiscal Q1.

Amit Daryanani - RBC Capital Markets - Analyst

Got it. And then could you just maybe talk about -- with the Juniper disengagement behind you now, does it impact the cash deposit base that you get from your customer? And could that potentially put some pressure on the cash cycle days that you would have to offset from better working capital management?

Ginger Jones - Plexus Corporation - SVP, CFO

It will reduce the cash deposit days, but it's really a one-to-one match with other days we have in either receivables or inventory. So net-net, I don't think it has a significant impact.

Amit Daryanani - RBC Capital Markets - Analyst

Got it, thank you.

Operator

Steven Fox, Cross Research.

Steven Fox - Cross Research - Analyst

Thanks, good morning. Two questions from me. First of all, you mentioned on the healthcare side a number of times I think share gains. And I was wondering if you could just expand on that a little bit. I'm sure you don't want to name what competitor you are taking share from, but generally what type of competitor you are picking up share from. And what kind of business is it in terms of end products and whether it's new or existing customers?

And then separately, Ginger, just so I'm clear, you ran some costs for the Wisconsin consolidation through the non-GAAP income statement in Q4. But are you expecting any costs to run through the Q1 income statement, outside of the charges that you called out? Thanks a lot.

Todd Kelsey - Plexus Corporation - EVP, COO

This is Todd. I will take the healthcare question here. First of all, if we look at where are we gaining share, of course, I'm not going to name names on this. But I mean I think it's balanced across what you'd call the major players, and then some smaller competitors as well.



But part of it is if you look at the performance and the revenue performance, particularly in F13 and our projections to F14, which you don't have great visibility to, but we are expecting good growth within this sector in fiscal 14 as well too.

The balance of customers, new versus existing, it is pretty balanced. We are adding new customers, and we tend to focus on market or industry leaders here. We are also gaining a lot of share with our existing customers. It was dominated our wins this quarter by existing customers, although a lot of it was with new divisions of existing customers. So in a way, we are broadening our penetration within these existing customers through the performance we are having with certain divisions.

Steven Fox - *Cross Research - Analyst*

I know you talked about different products sets that you are going after in healthcare. Is there anything that sort of you're doing better or worse in recently, when you look at the end products you are building?

Todd Kelsey - *Plexus Corporation - EVP, COO*

I would say the life sciences is an area of focus that's relatively new for us. So that is what we view as a major growth area. It also fits our mid to low volume, high-complexity strategy really well.

Ginger Jones - *Plexus Corporation - SVP, CFO*

Steve, I will take the second part of that question. In the September quarter, we did incur \$400,000 of costs related to the move of our Neenah facility. Because the amount was not material, we just absorbed that in our reported earnings. So as you can see on our income statement, we did not have a restructuring line or a special charges line for that in the fiscal 2013.

And just as a reminder, we also incurred about \$600,000 of Juniper disengagement costs in the June quarter.

So all in, we have absorbed about \$1 million of costs that you could have called special charges or restructuring in F13. In our mind, that was not significant enough to create a separate line. So we have absorbed that in our ongoing gross margin.

Looking forward to F14, we expect about \$3 million to \$4 million in the first half of the fiscal year from the Neenah consolidation. And I guided about \$1.5 million to \$2 million of that in the December quarter. We also -- although we are not guiding it today, we will have some costs in the second half of the fiscal year related to the startup of our Guadalajara facility, so it could be that we have some costs there that we would need to call out separately. We haven't estimated that yet.

Steven Fox - *Cross Research - Analyst*

Great, that's all very helpful. Thank you.

Operator

Mark Delaney, Goldman Sachs.



Mark Delaney - *Goldman Sachs - Analyst*

Great, thanks very much for taking the question. The question is on the gross margin line. I know there's a lot of different moving pieces as you guys have some new facilities in Europe, you are doing some work in Mexico and then also in Wisconsin. If you guys were at steady-state and you didn't have these different facilities that you are repositioning, where do you think gross margins would be?

Dean Foate - *Plexus Corporation - President, CEO*

That is a good question, but it would be in the double digits. Clearly, we've got a startup facility yet in Oradea -- that's Romania -- that while it's doing well is still a drag on our margin performance. And in fact, the EMEA region overall is still a drag because we've invested there intentionally with an expectation for longer-term growth. So it would be north of 10%.

If you'd ever get to the point where you weren't investing for the future -- but the reality is in our business, you have to have white space and capacity or you can't win any new business, because everybody wants to know where you are going to build their stuff. So that's just part of the model, and we have to manage that on an ongoing basis.

Mark Delaney - *Goldman Sachs - Analyst*

Okay, thank you for that. And then for my follow-up, you guys mentioned some weakness in the security part of your business. I was hoping you could elaborate a little bit more on that.

Dean Foate - *Plexus Corporation - President, CEO*

Yes, Todd commented -- that was, I think, specific to a single customer and their end markets. But they are a reasonably significant customer for us and an important one, and they just had to take their numbers down for (inaudible) reasons.

Mark Delaney - *Goldman Sachs - Analyst*

Thank you.

Operator

At this time, I am showing no further questions.

Dean Foate - *Plexus Corporation - President, CEO*

Well, that was pretty efficient. I guess we got through it all with our vast presentation material.

Operator

One moment, please. I do have additional questions that have queued. Thank you. Wamsi Mohan. Please go ahead with your question.

I will go ahead to the next queue. Sean Hannan, Needham & Company.

Sean Hannan - *Needham & Company - Analyst*

Yes, good morning. Thanks for taking my question. There were some comments I think that were made a little bit earlier in terms of strength you are seeing within wireless infrastructure, and also just being a general area that you are seeing strengthening for your general communications space. So I just want to see if you could expand on that a little bit for us, Dean or Todd, or whoever would like to comment, it would be helpful. Thanks.

Dean Foate - *Plexus Corporation - President, CEO*

Sure, we will let Todd take it.

Todd Kelsey - *Plexus Corporation - EVP, COO*

So basically, if you looked at Networking/Communications in general, it is still quite volatile. And I guess what I was highlighting is the one area -- there is one area where we are seeing some strength; it's around wireless infrastructure products. But other than that, it's a lot of ups and downs as far as end market is concerned.

Now, X Juniper, we are seeing good growth, but that's really primarily new program ramps, with a little bit of impact from wireless infrastructure.

Sean Hannan - *Needham & Company - Analyst*

Okay, and just to expand on that, is that really kind of a balance strength that you are seeing among your wireless infrastructure customers, or is it one or two, or how would you put that into context for us?

Dean Foate - *Plexus Corporation - President, CEO*

I would say it's a reasonably broad-based strength. That's a market with all the 4G rollouts that are going on that's relatively strong.

Sean Hannan - *Needham & Company - Analyst*

Okay, very helpful. Thank you.

Operator

Brian Alexander, Raymond James.

Brian Alexander - *Raymond James - Analyst*

Just a quick follow-up; I didn't want let you guys off the hook so easily. This one's easy, though. On the tax rate, Ginger, I think you said 8% to 10% for the fiscal year. What's the reason that's going up? Is that more regional mix and is that a level that you think will be sustainable beyond fiscal 2014 or might it come back down?



Ginger Jones - Plexus Corporation - SVP, CFO

Well, we had an unusual tax year this year in that we had several discrete tax items that benefited the tax rate and reduced it. Without those benefits, we would've been closer to 7.2% for the full year for fiscal 2013. So we are just projecting a more normal tax year in F14, and we think 8% to 10% is the right estimate. And I think that is a sustainable rate over the midterm.

Brian Alexander - Raymond James - Analyst

And then maybe just a little bit more color on your outlook for Coke and then the rest of your industrial commercial business. It sounded like you are saying a little bit more order volatility and softness across that customer base as we head into the December quarter. I don't want to put words in your mouth, but that's what it sounded like from the prepared remarks.

Dean Foate - Plexus Corporation - President, CEO

The Coca-Cola company asked us not to specifically comment on their program going forward and to defer all questions directly to them. So we are going to live up to that request. And I think given that its relative size of the program size relative to the rest of our business, which we've commented on in the past, I'm comfortable with that.

Relative to the rest of the Industrial/Commercial business, when you look at our December quarter, it tends to be, for some reason from a seasonality standpoint, a little bit more challenging quarter. And that's the way it appears to be unfolding at this point.

I don't know that this is anything that gives me a lot of surprise at the moment. It could be this is related to government shutdown concerns and just a lack of confidence in forecasting and uncertainty. I don't know. But it's a fairly broad-based reduction or decline across the customers, or softening at least in the near-term, before we start to see some improvement as we move further into the fiscal year.

Brian Alexander - Raymond James - Analyst

And then finally, is low- to mid-single digit revenue growth overall for the Company the way to think about fiscal 2014? Has that changed at all in the last three months?

Dean Foate - Plexus Corporation - President, CEO

No, it hasn't changed. It's a long road yet to get there, but if we are able to fulfill on the forecast that we have in front of us with new program wins, and if we assume the economy stays about at the kind of performance level that it's at now, we should be able to deliver that.

Brian Alexander - Raymond James - Analyst

Okay, thank you very much.

Operator

At this time, I am showing no further questions.

Dean Foate - Plexus Corporation - President, CEO

Okay. Well then, I guess we are really done. So first, to close out the fiscal year, again, as I said in my earlier commentary, it certainly wasn't the year we anticipated. It turned out to be a very challenging year. But I think we got a lot of the right things done.

I want to thank the shareholder base for putting their trust in our ability to manage through and overcome what was a very significant setback. And I'd also like to thank the Plexus folks, who really stay focused and professional, those involved directly in the setback, but also those elsewhere across the Company that really executed well and stayed focus on delivering for our customers.

So thanks to everyone, and thanks to the sell side and buy side that dialed into the call and asked questions today. Have a good day.

Operator

Thank you, ladies and gentlemen. This concludes the Plexus Corporation fiscal fourth quarter 2013 earnings announcement. You may now disconnect. Thank you for your participation.

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