KEMET CORP
Form 10-Q
February 01, 2018
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
FORM 10-Q
(Mark One)
ý QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended December 31, 2017
or
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to

Commission File Number: 001-15491

KEMET CORPORATION
(Exact name of registrant as specified in its charter)

DELAWARE	57-0923789
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

2835 KEMET WAY, SIMPSONVILLE, SOUTH CAROLINA 29681
(Address of principal executive offices, zip code)

(864) 963-6300
(Registrant's telephone number, including area code)

Former name, former address and former fiscal year, if changed since last report: N/A

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 ý NO o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). YES ý NO o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, 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 o	Accelerated filer x
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Emerging growth company o

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. o

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

The number of shares outstanding of the registrant’s common stock, par value $0.01 per share, as of January 30, 2018 was 56,605,329.

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KEMET CORPORATION AND SUBSIDIARIES
Form 10-Q for the Quarter ended December 31, 2017

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PART I - FINANCIAL INFORMATION
Item 1 - Financial Statements

KEMET CORPORATION AND SUBSIDIARIES
Condensed Consolidated Balance Sheets
(Amounts in thousands, except per share data)
(Unaudited)

	December 31, 2017	March 31, 2017
ASSETS		
Current assets:		
Cash and cash equivalents	$284,166	$109,774
Accounts receivable, net	140,239	92,526
Inventories, net	201,091	147,955
Prepaid expenses and other [(1)]	38,551	28,782
Total current assets	664,047	379,037
Property, plant and equipment, net of accumulated depreciation of $853,623 and $821,276 as of December 31, 2017 and March 31, 2017, respectively	374,719	209,311
Goodwill	40,294	40,294
Intangible assets, net	61,068	29,781
Equity method investments	8,750	63,416
Deferred income taxes [(1)]	11,922	8,367
Other assets	10,987	4,119
Total assets	$1,171,787	$734,325
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Current portion of long-term debt	$20,359	$2,000
Accounts payable	133,314	69,674
Accrued expenses	108,360	57,752
Income taxes payable	4,541	715
Total current liabilities	266,574	130,141
Long-term debt, less current portion	307,803	386,211
Other non-current obligations	152,718	60,131
Deferred income taxes	6,694	3,370
Stockholders' equity:		
Preferred stock, par value $0.01, authorized 10,000 shares, none issued	—	—
Common stock, par value $0.01, authorized 175,000 shares, issued 56,595 and 46,689 shares at December 31, 2017 and March 31, 2017, respectively	566	467
Additional paid-in capital	460,087	447,671
Retained earnings (deficit) [(1)]	242	(251,854)
Accumulated other comprehensive income	(22,897)	(41,812)
Total stockholders' equity	437,998	154,472
Total liabilities and stockholders' equity	$1,171,787	$734,325

[(1)] March 31, 2017 adjusted due to the adoption of Accounting Standards Update ("ASU") No. 2016-16, Income Taxes - Intra-Entity Transfers of Assets Other Than Inventory

See accompanying notes to the unaudited condensed consolidated financial statements.

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KEMET CORPORATION AND SUBSIDIARIES
Condensed Consolidated Statements of Operations
(Amounts in thousands, except per share data)
(Unaudited)

	Quarters Ended December 31,		Nine-Month Periods Ended December 31,	
	2017	2016	2017	2016
Net sales	$306,408	$188,029	$881,879	$560,272
Operating costs and expenses:				
Cost of sales [1]	213,947	140,551	629,905	423,526
Selling, general and administrative expenses [1]	47,751	26,520	125,799	78,119
Research and development [1]	10,005	7,013	29,057	20,956
Restructuring charges (credits)	3,530	(369)	6,536	4,317
(Gain) loss on write down and disposal of long-lived assets	(902)	132	(922)	6,500
Total operating costs and expenses	274,331	173,847	790,375	533,418
Operating income (loss)	32,077	14,182	91,504	26,854
Non-operating (income) expense:				
Interest income	(252)	(5)	(413)	(14)
Interest expense	7,407	9,918	25,732	29,751
Acquisition gains	(310)	—	(137,183)	—
Change in value of TOKIN option	—	(6,900)	—	3,500
Other (income) expense, net [1]	4,769	(3,052)	21,061	(5,627)
Income (loss) before income taxes and equity income (loss)	20,463	14,221	182,307	(756)
Income tax expense (benefit)	2,060	1,810	6,090	4,440
Income (loss) before equity income (loss)	18,403	12,411	176,217	(5,196)
Equity income (loss) from equity method investments	238	(133)	75,879	271
Net income (loss)	$18,641	$12,278	$252,096	$(4,925)
Net income (loss) per basic share	$0.33	$0.26	$4.91	$(0.11)
Net income (loss) per diluted share	$0.32	$0.22	$4.31	$(0.11)
Weighted-average shares outstanding:				
Basic	56,778	46,606	51,340	46,469
Diluted	58,937	55,296	58,431	46,469

[1] Quarter and nine-month period ended December 31, 2016 adjusted due to the adoption of ASU No. 2017-07, Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost

See accompanying notes to the unaudited condensed consolidated financial statements.

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KEMET CORPORATION AND SUBSIDIARIES
Condensed Consolidated Statements of Comprehensive Income (Loss)
(Amounts in thousands)
(Unaudited)

	Quarters Ended December 31,		Nine-Month Periods Ended December 31,	
	2017	2016	2017	2016
Net income (loss)	$18,641	$12,278	$252,096	$(4,925)
Other comprehensive income (loss):				
Foreign currency translation gains (losses)	6,503	(10,773)	20,301	(17,848)
Defined benefit pension plans, net of tax impact	147	165	(6)	492
Post-retirement plan adjustments	(47)	116	(141)	31
Equity interest in TOKIN’s other comprehensive income (loss)	(5)	6,161	5,568	598
Foreign exchange contracts	(5,330)	(1,166)	(6,807)	(2,872)
Other comprehensive income (loss)	1,268	(5,497)	18,915	(19,599)
Total comprehensive income (loss)	$19,909	$6,781	$271,011	$(24,524)

See accompanying notes to the unaudited condensed consolidated financial statements.

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KEMET CORPORATION AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows
(Amounts in thousands)
(Unaudited)

	Nine-Month Periods Ended December 31,	
	2017	2016
Net income (loss)	$252,096	$(4,925)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:		
Depreciation and amortization	36,694	27,971
Equity (income) loss from equity-method investments	(75,879)	(271)
Acquisition gains	(137,183)	—
Non-cash debt and financing costs	1,820	561
(Gain) loss on early extinguishment of debt	486	—
Stock-based compensation expense	4,837	3,471
Receivable write down	162	64
Change in value of TOKIN option	—	3,500
(Gain) loss on write down and disposal of long-lived assets	(922)	6,500
Pension and other post-retirement benefits	3,897	2,096
Change in deferred income taxes	(3,792)	819
Change in operating assets	26,296	21,459
Change in operating liabilities	(26,316)	(18,918)
Other	499	(183)
Net cash provided by (used in) operating activities	82,695	42,144
Investing activities:		
Capital expenditures	(30,925)	(15,011)
Acquisitions, net of cash received	167,129	—
Proceeds from sale of assets	1,227	—
Proceeds from dividend	2,731	—
Net cash provided by (used in) investing activities	140,162	(15,011)
Financing activities:		
Payments on revolving line of credit	(33,881)	—
Payments on long-term obligations	(361,625)	(2,428)
Proceeds from issuance of debt	334,978	—
Debt issuance costs	(5,002)	—
Purchase of treasury stock	—	(1,052)
Proceeds from exercise of stock warrants	8,838	—
Proceeds from exercise of stock options	5,122	69
Net cash provided by (used in) financing activities	(51,570)	(3,411)
Net increase (decrease) in cash and cash equivalents	171,287	23,722
Effect of foreign currency fluctuations on cash	3,105	(1,370)
Cash and cash equivalents at beginning of fiscal period	109,774	65,004
Cash and cash equivalents at end of fiscal period	$284,166	$87,356

See accompanying notes to the unaudited condensed consolidated financial statements.

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Notes to Condensed Consolidated Financial Statements
(Unaudited)

Note 1. Basis of Financial Statement Presentation

The condensed consolidated financial statements contained herein are unaudited and have been prepared from the books and records of KEMET Corporation and its subsidiaries ("KEMET" or the "Company"). In the opinion of management, the condensed consolidated financial statements reflect all adjustments, consisting only of normal recurring adjustments, necessary for a fair presentation of the results for the interim periods. The condensed consolidated financial statements have been prepared in accordance with the instructions to Form 10-Q, and therefore, do not include all information and footnotes necessary for a complete presentation of financial position, results of operations, and cash flows in conformity with U.S. generally accepted accounting principles ("U.S. GAAP"). Although the Company believes the disclosures are adequate to make the information presented not misleading, it is suggested that these condensed consolidated financial statements be read in conjunction with the audited financial statements and notes thereto included in the Company's Form 10-K for the fiscal year ended March 31, 2017 (the "Company's 2017 Annual Report").

The accompanying condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. In consolidation, all significant intercompany amounts and transactions have been eliminated. Certain prior year amounts have been reclassified to conform to current year presentation. Net sales and operating results for the quarter and nine-month periods ended December 31, 2017 are not necessarily indicative of the results to be expected for the full year.

The Company's significant accounting policies are presented in the Company's 2017 Annual Report.

Use of Estimates and Assumptions

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates, assumptions, and judgments based on historical data and other assumptions that management believes are reasonable. These estimates and assumptions affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements. In addition, they affect the reported amounts of revenues and expenses during the reporting period.

The Company's judgments are based on management's assessment as to the effect certain estimates, assumptions, or future trends or events may have on the financial condition and results of operations reported in the unaudited condensed consolidated financial statements. It is important that readers of these unaudited financial statements understand that actual results could differ from these estimates, assumptions, and judgments.

Recently Issued Accounting Pronouncements

In August 2017, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2017-12, Targeted Improvements to Accounting for Hedging Activities. The update amends and simplifies existing guidance in order to allow companies to more accurately present the economic effects of risk management activities in the financial statements. The effective date of this update is for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018, with early adoption permitted. The Company is currently evaluating the impact of the adoption of this guidance on the Company's consolidated financial statements.

In March 2017, the FASB issued ASU No. 2017-07, Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost. The update requires employers to report the service cost component in the same line item or items as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit cost are required to be presented in the income statement separately from the service cost component and outside a subtotal of Operating income. The Company states the other components of net benefit cost within Other (income) expense, net, on its Condensed Consolidated Statements of Operations. The effective date of this update is for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017, with early adoption permitted. The update requires retrospective application to all periods presented. The Company adopted this guidance in the first quarter of fiscal year 2018; the adoption of this guidance had an immaterial impact on the Company's condensed consolidated financial statements.

In January 2017, the FASB issued ASU No. 2017-04, Intangibles - Goodwill and Other. The update eliminates the requirement to calculate the implied fair value of goodwill to measure the amount of impairment loss, if any, under the second step of the current goodwill impairment test. Under the update, the goodwill impairment loss would be measured as the amount by which a reporting unit’s carrying value exceeds its fair value, not to exceed the carrying amount of goodwill. The effective

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date of this update is for annual reporting periods beginning after December 15, 2019, with early adoption permitted. The Company is currently evaluating the impact of the adoption of this guidance on the Company's consolidated financial statements, however the adoption of this guidance is not expected to have a significant effect on the Company's consolidated financial position, results of operations, or cash flows.

In October 2016, the FASB issued ASU No. 2016-16, Income Taxes - Intra-Entity Transfers of Assets Other Than Inventory. The update requires entities to recognize the income tax consequences of many intercompany asset transfers at the transaction date. The seller and buyer will immediately recognize the current and deferred income tax consequences of an intercompany transfer of an asset other than inventory. The tax consequences were previously deferred. The effective date of this update is for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017, with early adoption permitted. The update requires modified retrospective transition method which is a cumulative effect adjustment to retained earnings as of the beginning of the first effective reporting period. The Company adopted this guidance as of April 1, 2017 and recorded a cumulative effect adjustment to retained earnings of $203,000.

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230) Classification of Certain Cash Receipts and Cash Payments. The update clarifies how cash receipts and cash payments in certain transactions are presented and classified in the statement of cash flows. The effective date of this update is for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2017, with early adoption permitted. The update requires retrospective application to all periods presented but may be applied prospectively if retrospective application is impracticable. The Company is currently evaluating the impact of the adoption of this guidance on the Company's consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, Leases. The ASU requires lessees to recognize a right-of-use asset and a lease liability for virtually all of their leases (other than short-term leases). The guidance is to be applied using a modified retrospective approach at the beginning of the earliest comparative period in the financial statements. This ASU is effective for fiscal years and interim periods within those years beginning after December 15, 2018. Early application is permitted. The Company is currently in the process of assessing the impact the adoption of this guidance will have on the Company's consolidated financial statements.

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers, which supersedes existing accounting standards for revenue recognition and creates a single framework. The new guidance requires either a retrospective or a modified retrospective approach at adoption. Additional updates to Topic 606 issued by the FASB include the following:

- ASU No. 2015-14, Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date, which defers the effective date of the new guidance such that the new provisions will now be required for fiscal years, and interim periods within those years, beginning after December 15, 2017 (ASU No. 2015-14 is effective for the Company's fiscal year that begins on April 1, 2018 and interim periods within that fiscal year).
- ASU No. 2016-08, Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations, which clarifies the implementation guidance on principal versus agent considerations (reporting revenue gross versus net).
- ASU No. 2016-10, Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing, which clarifies the implementation guidance on identifying performance obligations and classifying licensing arrangements.
- ASU No. 2016-12, Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients, which clarifies the implementation guidance in a number of other areas.
- ASU No. 2016-20, Technical Corrections and Improvements to (Topic 606): Revenue from Contracts with Customers.
- ASU No. 2017-13, Revenue Recognition (Topic 605), Revenue from Contracts with Customers (Topic 606), Leases (Topic 840), and Leases (Topic 842): Provides additional implementation guidance on the previously issued ASU 2014-09.
- ASU No. 2017-14, Income Statement-Reporting Comprehensive Income (Topic 220), Revenue Recognition (Topic 605), and Revenue from Contracts with Customers (Topic 606). ASU 2017-14 includes amendments to certain SEC

paragraphs within the FASB Accounting Standards Codification.
The effective date of this guidance is for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018, with early adoption permitted, but not before the Company's fiscal year that began on April 1, 2017 (the original effective date of the ASU). The Company plans to adopt the requirements of the new standard in the first quarter of fiscal year 2019.

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The Company has completed the assessment phase, applied the principles of the new standard using the five step method to material customer contracts, and held discussions with key stakeholders and management. The Company is currently finalizing changes to accounting policies and internal controls over financial reporting. Key changes in the ASU that could potentially impact the Company’s revenue recognition include certain customer tooling contracts primarily within the original equipment manufacturers (“OEM”) channel and the deferral of incremental costs to fulfill a contract. The Company is currently finalizing the impact of the ASU on the consolidated results of operations, financial position, cash flows and financial statement disclosures.

There are currently no other accounting standards that have been issued that will have a significant impact on the Company’s financial position, results of operations or cash flows upon adoption.

Fair Value Measurement

The Company utilizes three levels of inputs to measure the fair value of (a) nonfinancial assets and liabilities that are recognized or disclosed at fair value in the Company’s consolidated financial statements on a recurring basis (at least annually) and (b) all financial assets and liabilities. Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. Valuation techniques used to measure fair value must maximize the use of observable inputs and minimize the use of unobservable inputs.

The first two inputs are considered observable and the last is considered unobservable. The levels of inputs are as follows:

- Level 1—Quoted prices in active markets for identical assets or liabilities.
- Level 2—Inputs other than Level 1 that are observable, either directly or indirectly, such as quoted prices for similar assets or liabilities, quoted prices in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.
- Level 3—Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

Assets and liabilities measured at fair value on a recurring basis as of December 31, 2017 and March 31, 2017 are as follows (amounts in thousands):

	Carrying Value December 31, 2017	Fair Value December 31, 2017	Fair Value Measurement Using			Carrying Value March 31, 2017	Fair Value March 31, 2017	Fair Value Measurement Using		
			Level 1	Level 2 (2)	Level 3			Level 1	Level 2 (2)	Level 3
Assets (Liabilities):										
Money markets (1)	$ 81,903	$ 81,903	$ 81,903	$ —	$ —	$ 2,055	$ 2,055	$ 2,055	$ —	$ —
Total debt	(328,162)	(344,661)	(338,898)	(5,763)	—	(388,211)	(385,251)	(353,000)	(32,251)	—
TOKIN option, net (3)	—	—	—	—	—	(9,900)	(9,900)	—	—	(9,900)

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(1) Included in the line item “Cash and cash equivalents” on the Condensed Consolidated Balance Sheets.

(2) The valuation approach used to calculate fair value was a discounted cash flow based on the borrowing rate for each respective debt facility.

(3) See Note 8, “Investment in TOKIN”, for a description of the TOKIN option, which was canceled on April 19, 2017 pursuant to the terms of the TOKIN Purchase Agreement as defined herein. The value of the option depended on the enterprise value of TOKIN and its forecasted EBITDA over the duration of the option. The option was valued using option pricing methods in a Monte Carlo simulation.

The table below summarizes TOKIN option valuation activity using significant unobservable inputs (Level 3) (amounts in thousands):

March 31, 2017	$ (9,900)
Option cancellation	9,900

December 31, 2017 $—

As discussed in Note 8, “Investment in TOKIN”, on April 19 2017 the TOKIN option was canceled pursuant to the terms of the TOKIN Purchase Agreement as defined herein.

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Inventories
Inventories are stated at the lower of cost or market. The components of inventories are as follows (amounts in thousands):

	December 31, 2017	March 31, 2017
Raw materials and supplies	$87,525	$65,750
Work in process	64,752	47,408
Finished goods	65,376	50,738
Subtotal	217,653	163,896
Inventory reserves	(16,562)	(15,941)
Inventories, net	$201,091	$147,955

Warrant
On September 11, 2017, K Equity sold the remaining portion of the Platinum Warrant to UBS Securities LLC (the "Underwriter"), in connection with the offering of 8,416,814 shares of the Company's common stock, at an offering price of $21.57 per share. The Company filed a registration statement on Form S-3 to register the offer and resale by K Equity of the shares. The Company did not receive any of the proceeds from the sale of the shares in the Offering, but received approximately $8.8 million from the Underwriter in connection with the cash exercise of the Platinum Warrant for all 8,416,814 shares underlying the Platinum Warrant at an exercise price of $1.05 per share.
As of December 31, 2017, K Equity does not have any outstanding warrants for shares of the Company's common stock.
Revenue Recognition
The Company ships products to customers based upon firm orders and revenue is recognized when the sales process is complete. This occurs when products are shipped to the customer in accordance with the terms of an agreement of sale, there is a fixed or determinable selling price, title and risk of loss have been transferred and collectability is reasonably assured. Based on product availability, customer requirements and customer consent, the Company may ship products earlier than the initial planned ship date. Shipping and handling costs are included in cost of sales.
A portion of sales is related to products designed to meet customer specific requirements. These products typically have stricter tolerances making them useful to the specific customer requesting the product and to customers with similar or less stringent requirements. The Company recognizes revenue when title to the products transfers to the customer.
A portion of sales is made to distributors under agreements allowing certain rights of return and price protection on unsold merchandise held by distributors. The Company's distributor policy includes inventory price protection and "ship-from-stock and debit" ("SFSD") programs common in the industry.
KEMET's SFSD program provides authorized distributors with the flexibility to meet marketplace prices by allowing them, upon a pre-approved case-by-case basis, to adjust their purchased inventory cost to correspond with current market demand. Requests for SFSD adjustments are considered on an individual basis, require a pre-approved cost adjustment quote from their local KEMET sales representative and apply only to a specific customer, part, specified special price amount, specified quantity, and are only valid for a specific period of time. To estimate potential SFSD adjustments corresponding with current period sales, KEMET records a sales reserve based on historical SFSD credits, distributor inventory levels, and certain accounting assumptions, all of which are reviewed quarterly.
Most of the Company's distributors have the right to return to KEMET a certain portion of the purchased inventory, which, in general, does not exceed 6% of their purchases from the previous fiscal quarter. KEMET estimates future returns based on historical return patterns and records a corresponding allowance on the Condensed Consolidated Balance Sheets. The Company also offers volume based rebates on a case-by-case basis to certain customers in each of the Company's sales channels.
The establishment of sales allowances is recognized as a component of the line item "Net sales" on the Condensed Consolidated Statements of Operations, while the associated reserves are included in the line item "Accounts receivable, net" on the Condensed Consolidated Balance Sheets. Estimates used in determining sales allowances are

subject to various factors. This includes, but is not limited to, changes in economic conditions, pricing changes, product demand, inventory levels in the supply chain, the effects of technological change, and other variables that might result in changes to the Company's estimates.

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The Company provides a limited warranty to customers that the Company’s products meet certain specifications. The warranty period is generally limited to one year, and the Company’s liability under the warranty is generally limited to a replacement of the product or refund of the purchase price of the product. Warranty costs as a percentage of net sales were less than 1.0% for the quarters and nine-month periods ended December 31, 2017 and 2016. The Company recognizes warranty costs when they are both probable and reasonably estimable.

Note 2. Acquisitions

Sale of Electro-Mechanical Business and Acquisition of Remaining Interest in TOKIN

Between February 1, 2013 and April 19, 2017, KEMET, through its wholly-owned subsidiary, KEMET Electronics Corporation (“KEC”), held a 34% economic interest in TOKIN Corporation (“TOKIN”) pursuant to a Stock Purchase Agreement (the “Stock Purchase Agreement”) by and among KEC, TOKIN and NEC Corporation (“NEC”), as calculated based on the number of common shares held by KEC, directly and indirectly, in proportion to the aggregate number of common and preferred shares of TOKIN outstanding as of such date. TOKIN was established in Japan in 1938 and is engaged in production and distribution of tantalum capacitors, transmitting communication devices, magnetic devices, piezoelectric devices and sensors. TOKIN has six manufacturing locations throughout Asia and was previously operating as a joint venture with NEC.

On April 14, 2017, TOKIN closed on the sale of its electro-mechanical devices (“EMD”) business to NTJ Holdings 1 Ltd. (“NTJ”), a special purpose entity that is owned by funds managed or operated by Japan Industrial Partners, Inc. (“JIP”), pursuant to a master sale and purchase agreement (the “EMD Master Sale and Purchase Agreement”) previously entered into between TOKIN, NTJ and JIP (“Sale of EMD”). The initial selling price for EMD was JPY 48.2 billion, or approximately $431.0 million, using the March 31, 2017 exchange rate of 111.823 Japanese Yen to 1.00 U.S. Dollar, and is subject to certain working capital adjustments pursuant to the EMD Master Sale and Purchase Agreement. At the closing of the Sale of EMD, TOKIN used a portion of the sale proceeds to repay debt related to a shareholder loan from NEC. The TOKIN historical balance sheet was adjusted to reflect the removal of net assets sold and other items directly impacted by the Sale of EMD. Additionally, due to KEMET’s 34% equity interest in TOKIN held as of the closing, adjustments have been made to reflect KEMET’s accounting for the Sale of EMD in accordance with the equity method of accounting.

On April 19, 2017, pursuant to a stock purchase agreement (the “TOKIN Purchase Agreement”) dated February 23, 2017 between KEC and NEC, KEC completed its acquisition, subject to final purchase price adjustment, of the remaining 66% economic interest in TOKIN, and as a result, TOKIN is now a 100% owned indirect subsidiary of KEMET (the “TOKIN Acquisition”). Under the terms of the TOKIN Purchase Agreement, KEC paid NEC JPY 16.2 billion, or approximately $148.6 million (using the April 19, 2017 exchange rate of 109.007 Japanese Yen to 1.00 U.S. Dollar), for all of the outstanding shares of TOKIN it did not already own. The preliminary purchase price was comprised of JPY 6.0 billion, or approximately $55.0 million (using the April 19, 2017 exchange rate of 109.007 Japanese Yen to 1.00 U.S. Dollar) plus JPY 10.2 billion, or approximately $93.6 million, which represented one-half of the estimated excess net cash proceeds (“Excess Cash”) from the Sale of EMD. The acquisition price is subject to working capital adjustments pursuant to the EMD Master Sale and Purchase Agreement. As a result of these working capital adjustments, the acquisition price was increased by JPY 0.3 billion, or approximately $3.0 million (using the September 30, 2017 exchange rate of 112.502 Japanese Yen to 1.00 U.S. Dollar) in the second quarter of fiscal year 2018. No additional working capital adjustments were recorded in the third quarter of fiscal year 2018.

The Company believes the acquisition of TOKIN will expand KEMET’s geographic presence, combining KEMET’s presence in the western hemisphere and TOKIN’s excellent position in Asia to enhance customer reach and create an entrance into Japan for KEMET. The Company believes TOKIN’s product portfolio is a strong complement to KEMET’s existing product portfolio. KEMET believes the combination creates a leader in the combined polymer and tantalum capacitors market. The acquisition also enhances KEMET’s product diversification with entry into Electro-Magnetic Compatible components ("EMC") as well as sensors and actuators. With the increased scale, the Company anticipates optimizing costs through competitive raw materials sourcing and maximizing operating efficiencies. Consistent with expectations, the acquisition has been accretive to earnings with improvement in Net income, Adjusted EBITDA and cash flow. TOKIN’s tantalum capacitor business is included within KEMET’s Solid

Capacitor segment ("Solid Capacitors") and the remainder of TOKIN's business formed a new reportable segment for KEMET, Electro-magnetic, Sensors & Actuators ("MSA").

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The following table shows the preliminary components of the acquisition price: (amounts in thousands):

Upfront cash consideration [1]	$148,614
Acquisition payable [2]	3,144
Indemnity asset [3]	8,500
Less: Put option [4]	(9,900)
Net consideration transferred	$150,358

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[1] The upfront cash payment is comprised of JPY 6.0 billion plus one half of Excess Cash in an amount of approximately JPY 10.2 billion, approximately $55.0 million and $93.6 million (using the April 19, 2017 exchange rate of 109.007 Japanese Yen to 1.00 U.S. Dollar), respectively.
[2] Current estimate of the additional amount due to NEC Corporation upon the settlement of the adjusted purchase price for the EMD sale.
[3] Pursuant to the Stock Purchase Agreement between KEMET and NEC, NEC was required to indemnify TOKIN and/or KEC for any breaches by TOKIN or NEC of certain representations, warranties and covenants in the Stock Purchase Agreement. NEC's aggregate liability for indemnification claims was limited to $25.0 million. Prior to the acquisition, KEMET's equity method investment balance included an $8.5 million indemnification asset pursuant to this indemnification arrangement. In connection with the TOKIN Acquisition, NEC was released from its indemnification obligations to KEMET without an exchange of consideration; as such, this amount of released obligation is included as purchase consideration by KEMET.
[4] Pursuant to the option agreement, dated as of March 12, 2012, by and among NEC and KEMET (the "Option Agreement"), from April 1, 2015 through May 31, 2018, NEC had the right to require KEC to purchase all outstanding capital stock of TOKIN (the "Put Option"). The fair value of the Put Option of $9.9 million was reflected as a liability on KEMET's balance sheet prior to KEMET's acquisition of the remaining 66% economic interest in TOKIN. The Put Option was canceled, pursuant to the terms of the TOKIN Purchase Agreement with no exchange of consideration between NEC and KEMET. Accordingly, the fair value of the Put Option reduces the amount of consideration paid to acquire NEC's equity in TOKIN.

In accordance with ASC 805, KEMET's previously held 34% equity interest in TOKIN and the assets acquired and the liabilities assumed have been measured at their fair values based on various preliminary estimates. The preliminary acquisition-date fair value of KEMET's previously held 34% equity interest in TOKIN is approximately $206.0 million, which was derived from 34% of the fair value of TOKIN as of April 19, 2017 derived from the discounted cash flow method.

The following table presents the preliminary allocations of the aggregate purchase price based on the estimated fair values of the assets and liabilities (amounts in thousands):

	Fair Value
Cash	$315,743
Accounts Receivable	79,295
Inventory	35,310
Other current assets	20,902
Property, Plant and equipment [1]	154,961
Intangible assets [1][2]	33,025
Equity method investments [1]	11,128
Other assets	8,617
Current portion of long term debt	(3,225)
Accounts payable	(81,642)
Accrued expenses	(46,276)
Other non-current obligations	(103,486)
Deferred income taxes [1]	(1,419)
Total net assets acquired	$422,933

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(1) Amount revised in the third quarter of fiscal year 2018; however, the values are still preliminary.
(2) Includes trade name for $8.0 million and products and relationships of $25.0 million. TOKIN’s technology, products, and relationships were valued as a grouped, composite intangible asset due to the Company’s products being dependent on the existing technology, which enabled a product portfolio that customers found appealing in selecting and designing electronic components for purchase. The trade name was valued based on the relief from royalty method and have indefinite remaining useful life. The products and relationships were valued on the excess earnings method and are amortized over 10 years.

There were $0.8 million of acquisition-related costs, which were all recognized as an expense in the line item “Selling, general and administrative expenses” on the Condensed Consolidated Statements of Operations in the nine-month period ended December 31, 2017.

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The above allocation of purchase price has been prepared based on preliminary estimates; the final amounts recorded may differ materially from the information presented herein. These estimates are subject to change pending further review of the acquired business. The following components of the initial valuation are still preliminary: deferred income taxes, equity method investments, products and relationships, property plant and equipment for some locations, and management continues to assess the bargain gain in accordance with ASC 805. In the quarter ended December 31, 2017, property, plant and equipment was reduced by $4.6 million, equity method investments decreased by $1.7 million, intangible assets decreased by $0.3 million and the value of the deferred income tax liability was decreased $6.9 million due to additional adjustments made to record property, plant and equipment and equity method investments at fair value. A change in the fair value of assets acquired or liabilities assumed in the merger from those preliminary valuations presented above would result in a corresponding change in the amount of bargain purchase gain that resulted from the merger in a business combination when the fair value of net assets acquired exceeds the sum of consideration transferred and the fair value of the acquirer's previously held interest in the acquiree. The gain is recognized immediately in earnings in accordance with U.S. GAAP.

The following table reflects the preliminary bargain purchase gain resulting from the TOKIN Acquisition (amounts in thousands):

Net consideration transferred	$150,358
Preliminary fair value of KEMET's previously held equity interest in TOKIN[1]	205,952
Less: Preliminary fair value of net assets acquired	(422,933)
Bargain purchase gain	$(66,623)

(1) Value based in the 34% of the enterprise value determined under the discounted cash flow method.

The gain is included in the line item "Acquisition gains" in the Condensed Consolidated Statements of Operations.

Pro Forma Results

The following table summarizes, on a pro forma basis, the combined results of operations of the Company and TOKIN as though the acquisition and the sale of EMD had occurred as of April 1, 2016. The pro forma amounts presented are not necessarily indicative of either the actual consolidated results had the acquisition occurred as of April 1, 2016, or of future consolidated operating results (amounts in thousands, except per share data):

	Quarters Ended December 31,		Nine-Month Periods Ended December 31,	
	2017	2016	2017 [1]	2016 [2]
Pro forma revenues	$306,408	$263,260	$899,353	$785,388
Pro forma net income (loss) from continuing operations available to common stockholders	19,009	(4,484)	44,741	243,746
Pro forma earnings per common share - basic	0.33	(0.10)	0.87	5.25
Pro forma earnings per common share - diluted	0.32	(0.10)	0.77	4.51
Pro forma common shares - basic	56,778	46,606	51,340	46,469
Pro forma common shares - diluted	58,937	46,606	58,431	53,990

[1] The net income for the nine-month period ended December 31, 2017 excludes the following: 34% of the preliminary gain on sale of the EMD business of $75.2 million, the preliminary gain related to the fair value of KEMET's previous 34% interest in TOKIN of $70.6 million, and the preliminary bargain gain on the acquisition of TOKIN of $66.6 million.

[2] The net income for the nine-month period ended December 31, 2016 includes the following: 34% of the preliminary gain on sale of the EMD business of $123.4 million (which includes the release of a valuation allowance that was recorded in the fourth quarter of fiscal year 2017 and the use of the deferred tax asset which was recorded in the first quarter of fiscal year 2018), the preliminary gain related to the fair value of KEMET's previous 34% interest in TOKIN of $68.5 million, and the preliminary bargain gain on the acquisition of TOKIN of $64.6 million.

Note 3. Debt

A summary of debt is as follows (amounts in thousands):

	December 31, 2017	March 31, 2017
Term Loan Credit Agreement [(1)]	$ 322,540	$—
10.5% Senior Notes, net [(2)]	—	352,472
Revolving line of credit	—	33,881
Other [(3)]	5,622	1,858
Total debt	328,162	388,211
Current maturities	(20,359)	(2,000)
Total long-term debt	$ 307,803	$386,211

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[(1)] Amounts shown are net of discount, bank issuance costs and other indirect issuance costs of $13.8 million and zero as of December 31, 2017 and March 31, 2017, respectively which reduce the Term Loan Credit Agreement (as defined herein) balance.

[(2)] Amounts shown are net of premium and debt issuance costs of zero and $0.5 million as of December 31, 2017 and March 31, 2017, respectively, which reduce the 10.5% Senior Notes balance.

[(3)] The amount shown is net of discount of $0.5 million at both December 31, 2017 and March 31, 2017.

The line item “Interest expense” on the Condensed Consolidated Statements of Operations for the quarters and nine-month periods ended December 31, 2017 and 2016, consists of the following (amounts in thousands):

	Quarters Ended December 31,		Nine-Month Periods Ended December 31,	
	2017	2016	2017	2016
Contractual interest expense	$6,680	$9,693	$23,762	$29,091
Capitalized interest	(41)	(48)	(80)	(151)
Amortization of debt issuance costs	98	348	410	1,044
Amortization of debt (premium) discount	570	(204)	1,326	(603)
Imputed interest on acquisition-related obligations	28	39	84	120
Interest expense on capital lease	72	90	230	250
Total interest expense	$7,407	$9,918	$25,732	$29,751

10.5% Senior Notes

On April 28, 2017, the Company repurchased and retired the full outstanding balance of $353.0 million of its 10.5% Senior Notes due May 1, 2018 (the “10.5% Senior Notes”). The Company had interest payable related to the 10.5% Senior Notes included in the line item “Accrued expenses” on its Condensed Consolidated balance sheets of zero and $15.4 million as of December 31, 2017 and March 31, 2017, respectively.

Term Loan Credit Agreement

On April 28, 2017, KEMET entered into a Term Loan Credit Agreement (the “Term Loan Credit Agreement”) by and among the Company, KEC (together with the Company, the “Borrowers”), Bank of America, N.A. as the Administrative Agent and Collateral Agent, Merrill Lynch, Pierce, Fenner & Smith Incorporated, as sole lead arranger and bookrunner and various other lenders thereto from time to time.

The Term Loan Credit Agreement provides for a $345 million term loan facility. In addition, the Borrowers may request incremental term loan commitments in an aggregate amount not to exceed $50 million (together with the initial $345 million term loan, the “Term Loans”). The proceeds were used, together with cash on hand, to fund the redemption of all of KEMET’s outstanding 10.5% Senior Notes, which were also called for redemption on April 28, 2017. The Term Loans were made with an original issue discount of 300 basis points. At the Company’s election, the Term Loans may be made as either Base Rate Term Loans or LIBO Rate Term Loans (each as defined in the Term Loan Credit Agreement). The applicable margin for term loans is 5.0% for Base Rate Term Loans and 6.0% for LIBO Rate Term Loans. All LIBO Rate Term Loans are subject to a pre-margin floor of 1.00%. The Term Loan Credit

Agreement contains customary covenants and events of default.

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The Company also entered into the Term Loan Security Agreement dated as of April 28, 2017 (the "Security Agreement"), by and among the Company, KEC and certain other subsidiaries of the Company and Bank of America, N.A., as collateral agent, pursuant to which the Company's obligations under the Term Loan Credit Agreement are secured by a pledge of 65% of the outstanding voting stock of certain first-tier subsidiaries organized in Italy, Japan, Mexico and Singapore, and a second lien pledge on the collateral securing KEMET's revolving credit facility. The obligations of the Company under the Term Loan Credit Agreement are guaranteed by certain of its subsidiaries, including KRC Trade Corporation, KEMET Services Corporation, KEMET Blue Powder Corporation and The Forest Electric Company. The Term Loans mature April 28, 2024, and may be extended in accordance with the Term Loan Credit Agreement. The Company may prepay loans under the Term Loan Credit Agreement at any time, subject to certain notice requirements and certain prepayment premiums during the first two years. Pursuant to the terms of the Term Loan Credit Agreement, the Company is required to make quarterly principal payments equal to 1.25% of the aggregate principal amount on the initial $345 million term loan. The Company made a quarterly principal payment of 1.25% or $4.3 million, during the month of December 2017.

The Company currently pays interest on the Term Loan Security Agreement on a monthly basis due to favorable LIBO rates, and as such had only three days interest payable related to the Term Loan Security Agreement included in the line item "Accrued expenses" on its Condensed Consolidated balance sheets of $0.2 million and zero as of December 31, 2017 and March 31, 2017.

Revolving Line of Credit

In connection with the closing of the new Term Loan Credit Agreement, KEC also entered into Amendment No. 9 to Loan and Security Agreement, Waiver and Consent, dated as of April 28, 2017, by and among KEC, the other borrowers named therein, the financial institutions party thereto as lenders and Bank of America, N.A., as agent for the lenders (the "Loan Amendment"). The Loan Amendment increases the facility amount to $75.0 million and provides KEC with lower applicable interest rate margins and the ability to complete the refinancing. As part of the overall refinancing, KEC also repaid all amounts outstanding under the Loan Amendment.

As of December 31, 2017, there were no borrowings under the revolving line of credit, and the Company's available borrowing capacity, which is based on factors including outstanding eligible accounts receivable, inventory and equipment collateral, under the Loan and Security Agreement was $65.1 million.

Other Debt

In January 2017, KEMET's wholly-owned subsidiary, KEMET Electronics Portugal, S.A., received the first part of an interest free loan from the Portuguese Government in the amount of EUR 2.2 million (or $2.5 million) to be used for fixed asset purchases. In July 2017, KEMET Electronics Portugal, S.A. received the second part of the loan in the amount of EUR 277 thousand (or $325 thousand). The loan has a total term of eight years ending February 1, 2025. The loan will be repaid through semi-annual payments beginning on August 1, 2019. The first payment will be in the amount of EUR 185 thousand (or $211 thousand) beginning on August 1, 2019 and the remaining payments will be in the amount of EUR 210 thousand (or $248 thousand). Since the debt is non-interest bearing, we have recorded a debt discount in the amount of EUR 0.5 million (or $0.6 million) with an offsetting reduction to fixed assets. This discount will be amortized over the life of the loan through interest expense. If certain conditions are met, such as increased headcount, increased revenue and increased gross value added, a portion of the loan could be forgiven during fiscal year 2020.

In September 2017, TOKIN received a short term borrowing pursuant to an overdraft agreement with The 77 Bank Limited, located in Japan, in the amount of 350 million yen (or $3.1 million), at an interest rate of 0.53% (JBA TIBOR + 40 basis points). The loan is due September 2018, and the loan agreement automatically renews if both parties choose not to terminate or modify it.

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Note 4. Goodwill and Intangible Assets

The following table highlights the Company’s intangible assets (amounts in thousands):

	December 31, 2017			March 31, 2017		
	Carrying Amount	Accumulated Amortization	Net Amount	Carrying Amount	Accumulated Amortization	Net Amount
Indefinite Lived Intangible Assets:						
Trademarks	$15,024	$ —	$15,024	$7,207	$ —	$7,207
Amortizing Intangibles:						
Purchased technology, customer relationships and patents (2 - 21 years)	69,058	23,014	46,044	39,527	16,953	22,574
	$84,082	$ 23,014	$61,068	$46,734	$ 16,953	$29,781

For the quarters ended December 31, 2017 and 2016, amortization related to intangibles was $1.1 million and $0.5 million, respectively. For the nine-month periods ended December 31, 2017 and 2016, amortization related to intangibles was $3.4 million and $1.6 million, respectively. The weighted-average useful life of amortized intangibles was 14.1 years and 16.7 years as of December 31, 2017 and 2016, respectively. The KEMET Blue Powder patent was renewed in October 2017, and the next renewal will take place in October 2021. Estimated amortization of intangible assets for each of the next five fiscal years is $4.6 million.

The changes in the carrying amount of goodwill for the nine-month period ended December 31, 2017 are as follows (amounts in thousands):

	Corporate	Solid Capacitors	Film and Electrolytic	Total
Gross balance as of March 31, 2017				
Goodwill	$ 4,710	$ 35,584	$ 1,092	$41,386
Accumulated impairment losses				