

METHODE ELECTRONICS INC

Form 10-Q

September 11, 2008

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549**

**FORM 10-Q**

**(Mark One)**

- Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended August 2, 2008**
- or**
- Transition Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.**

**Commission file number 0-2816  
METHODE ELECTRONICS, INC.**

(Exact name of registrant as specified in its charter.)

Delaware

36-2090085

(State or other jurisdiction of  
incorporation or organization)

(I.R.S. Employer  
Identification No.)

7401 West Wilson Avenue, Harwood Heights, Illinois

60706-4548

(Address of principal executive offices)

(Zip Code)

(Registrant's telephone number, including area code) (708) 867-6777

None

(Former name, former address, former fiscal year, if changed since last report)

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

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company   
(Do not check if a smaller reporting company)

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

At September 9, 2008, Registrant had 38,478,998 shares of common stock outstanding.

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## PART I FINANCIAL INFORMATION

## Item 1 Financial Statements

## METHODE ELECTRONICS, INC AND SUBSIDIARIES

## CONDENSED CONSOLIDATED BALANCE SHEETS

(in thousands)

|  | August 2,<br>2008<br>(Unaudited) | May 3, 2008    |
|--|----------------------------------|----------------|
| <b>ASSETS</b>                              |                                  |                |
| <b>CURRENT ASSETS</b>                      |                                  |                |
| Cash and cash equivalents                  | \$ 111,488                       | \$ 104,716     |
| Accounts receivable, net                   | 74,172                           | 85,805         |
| Inventories:                               |                                  |                |
| Finished products                          | 14,783                           | 15,384         |
| Work in process                            | 18,821                           | 20,715         |
| Materials                                  | 21,825                           | 19,850         |
|  | 55,429                           | 55,949         |
| Deferred income taxes                      | 8,885                            | 8,730          |
| Prepaid expenses and other current assets  | 7,557                            | 6,028          |
| <b>TOTAL CURRENT ASSETS</b>                | <b>257,531</b>                   | <b>261,228</b> |
| <b>PROPERTY, PLANT AND EQUIPMENT</b>       | <b>314,482</b>                   | <b>308,264</b> |
| Less allowances for depreciation           | 225,944                          | 217,984        |
|  | 88,538                           | 90,280         |
| <b>GOODWILL</b>                            | <b>54,476</b>                    | <b>54,476</b>  |
| <b>INTANGIBLE ASSETS, net</b>              | <b>40,046</b>                    | <b>41,282</b>  |
| <b>OTHER ASSETS</b>                        | <b>27,314</b>                    | <b>23,365</b>  |
|  | 121,836                          | 119,123        |
|  | \$ 467,905                       | \$ 470,631     |
| <b>LIABILITIES AND SHAREHOLDERS EQUITY</b> |                                  |                |
| <b>CURRENT LIABILITIES</b>                 |                                  |                |
| Accounts payable                           | \$ 33,808                        | \$ 42,810      |
| Other current liabilities                  | 33,598                           | 34,313         |
| <b>TOTAL CURRENT LIABILITIES</b>           | <b>67,406</b>                    | <b>77,123</b>  |
| <b>OTHER LIABILITIES</b>                   | <b>14,635</b>                    | <b>13,833</b>  |
| <b>DEFERRED COMPENSATION</b>               | <b>5,483</b>                     | <b>6,890</b>   |
| <b>SHAREHOLDERS EQUITY</b>                 |                                  |                |

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|   |            |            |
|---|------------|------------|
| Common stock, \$0.50 par value, 100,000,000 shares authorized, 38,281,965<br>and 38,225,379 shares issued as of August 2, 2008 and May 3, 2008,<br>respectively | 19,141     | 19,113     |
| Unearned common stock issuances   | (4,257)    | (4,257)    |
| Additional paid-in capital  | 70,865     | 69,953     |
| Retained earnings   | 270,759    | 265,838    |
| Accumulated other comprehensive income  | 30,116     | 28,381     |
| Treasury stock, 702,708 shares as of August 2, 2008 and May 3, 2008   | (6,243)    | (6,243)    |
|   | 380,381    | 372,785    |
|   | \$ 467,905 | \$ 470,631 |

See notes to condensed consolidated financial statements.

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METHODE ELECTRONICS, INC. AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED STATEMENTS OF INCOME (Unaudited)  
 (in thousands, except per share data)

|   | Three Months Ended |                 |
|---|--------------------|-----------------|
|   | August 2,<br>2008  | July 28, 2007   |
| <b>INCOME</b>   |                    |                 |
| Net sales   | \$ 134,514         | \$ 125,009      |
| Other   | 733                | 146             |
|   | 135,247            | 125,155         |
| <b>COSTS AND EXPENSES</b>                                 |                    |                 |
| Cost of products sold                                     | 105,430            | 98,335          |
| Restructuring   | 4,917              |                 |
| Selling and administrative expenses                       | 16,452             | 15,964          |
|   | 126,799            | 114,299         |
| Income from operations                                    | 8,448              | 10,856          |
| Interest income, net                                      | 534                | 436             |
| Other, net  | (269)              | (220)           |
| Income before income taxes                                | 8,713              | 11,072          |
| Income taxes  | 1,897              | 2,800           |
| <b>NET INCOME</b>   | <b>\$ 6,816</b>    | <b>\$ 8,272</b> |
| Amounts per common share:                                 |                    |                 |
| Basic net income  | \$ 0.18            | \$ 0.22         |
| Diluted net income  | \$ 0.18            | \$ 0.22         |
| Cash dividends:   |                    |                 |
| Common stock  | \$ 0.05            | \$ 0.05         |
| Weighted average number of Common Shares outstanding:     |                    |                 |
| Basic   | 37,198             | 36,993          |
| Diluted   | 37,644             | 37,491          |
| See notes to condensed consolidated financial statements. |                    |                 |

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METHODE ELECTRONICS, INC. AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)  
 (in thousands)

|   | Three Months Ended |                  |
|---|--------------------|------------------|
|   | August 2,<br>2008  | July 28, 2007    |
| <b>OPERATING ACTIVITIES</b>   |                    |                  |
| Net income  | \$ 6,816           | \$ 8,272         |
| Adjustments to reconcile net income to net cash provided by operating activities: |                    |                  |
| Provision for depreciation  | 5,942              | 4,746            |
| Amortization of intangibles   | 1,372              | 1,330            |
| Amortization of stock awards and stock options                                    | 792                | 426              |
| Changes in operating assets and liabilities                                       | (3,722)            | 4,735            |
| Other   | 142                | 73               |
| <b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>                                  | <b>11,342</b>      | <b>19,582</b>    |
| <b>INVESTING ACTIVITIES</b>   |                    |                  |
| Purchases of property, plant and equipment  | (3,340)            | (4,656)          |
| Acquisition of businesses   |                    | (668)            |
| Acquisition of technology licenses  | (156)              | (346)            |
| Joint venture dividend  |                    | (1,000)          |
| Other   | 63                 | (181)            |
| <b>NET CASH USED IN INVESTING ACTIVITIES</b>                                      | <b>(3,433)</b>     | <b>(6,851)</b>   |
| <b>FINANCING ACTIVITIES</b>   |                    |                  |
| Proceeds from exercise of stock options   | 103                | 1,016            |
| Tax benefit from stock options and awards   | 46                 | 129              |
| Cash dividends  | (1,895)            | (1,884)          |
| <b>NET CASH USED IN FINANCING ACTIVITIES</b>                                      | <b>(1,746)</b>     | <b>(739)</b>     |
| Effect of foreign currency exchange rate changes on cash                          | 609                | 186              |
| <b>INCREASE IN CASH AND CASH EQUIVALENTS</b>                                      | <b>6,772</b>       | <b>12,178</b>    |
| Cash and cash equivalents at beginning of period                                  | 104,716            | 60,091           |
| <b>CASH AND CASH EQUIVALENTS AT END OF PERIOD</b>                                 | <b>\$ 111,488</b>  | <b>\$ 72,269</b> |

See notes to condensed consolidated financial statements.

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**METHODE ELECTRONICS, INC. AND SUBSIDIARIES**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)**  
(Dollar amounts in thousands, except share data)

August 2, 2008

**1. BASIS OF PRESENTATION**

Methode Electronics, Inc. was incorporated in 1946 as an Illinois corporation and reincorporated in Delaware in 1966. As used herein, we, us, our, the Company or Methode means Methode Electronics, Inc. and its subsidiaries. The condensed consolidated financial statements and related disclosures as of August 2, 2008 and results of operations for the three months ended August 2, 2008 and July 28, 2007 are unaudited, pursuant to the rules and regulations of the Securities and Exchange Commission ( SEC ). The May 3, 2008 condensed consolidated balance sheet was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America ( U.S. GAAP ). Certain information and footnote disclosures normally included in the financial statements prepared in accordance with U.S. GAAP have been condensed or omitted pursuant to such rules and regulations. In our opinion, these financial statements include all adjustments (consisting only of normal recurring adjustments) necessary for the fair statement of the results for the interim periods. These financial statements should be read in conjunction with the financial statements included in our latest Form 10-K for the year ended May 3, 2008 filed with the SEC on July 17, 2008. Results may vary from quarter to quarter for reasons other than seasonality.

**2. RECENT ACCOUNTING PRONOUNCEMENTS**

We adopted Financial Accounting Standards Board ( FASB ) Statement of Financial Accounting Standard ( SFAS ) No. 157, Fair Value Measurements ( SFAS No. 157 ) on May 4, 2008 for financial assets and liabilities, and non-financial assets and liabilities that are recognized or disclosed at fair value in the financial statements on a recurring basis. SFAS No. 157 defines fair value, establishes a framework for measuring fair value as required by other accounting pronouncements and expands fair value measurement disclosures. The provisions of SFAS No. 157 are applied prospectively upon adoption and did not have a material impact on our condensed consolidated financial statements. The disclosures required by SFAS No. 157 are included in Note 12, Fair Value Measurements, to our condensed consolidated financial statements.

In February 2008, the FASB issued FASB Staff Position No. 157-2, which delays the effective date of SFAS No. 157 for non-financial assets and liabilities, which are not measured at fair value on a recurring basis (at least annually) until fiscal years beginning after November 15, 2008, which is our fiscal year 2010 that begins May 3, 2009. We are currently assessing the impact of adopting SFAS No. 157 for non-financial assets and liabilities on our condensed consolidated financial statements.

We adopted SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of FASB Statement No. 115 ( SFAS No. 159 ) as of May 4, 2008. SFAS No. 159 permits entities to elect to measure many financial instruments and certain other items at fair value. We did not elect the fair value option for any assets or liabilities, which were not previously carried at fair value. Accordingly, the adoption of SFAS No. 159 had no impact on our condensed consolidated financial statements.

The Company adopted Emerging Issues Task Force (EITF) No. 06-4, Accounting for Deferred Compensation and Postretirement Benefit Aspects of Endorsement Split-Dollar Life Insurance Arrangements ( EITF No. 06-4 ) as of May 4, 2008. EITF No. 06-4 requires that endorsement split-dollar life insurance arrangements, which provide a benefit to an employee beyond the postretirement period be recorded in accordance with SFAS No. 106, Employer's Accounting for Postretirement Benefits Other Than Pensions or APB Opinion No. 12, Omnibus Opinion 1967 based on the substance of the agreement with the employee. The adoption of EITF No. 06-4 had no impact on our condensed consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141 (revised 2007) ( SFAS No. 141R ), a revision of SFAS No. 141, Business Combinations. SFAS No. 141R establishes requirements for the recognition and measurement of acquired assets, liabilities, goodwill and non-controlling interests. SFAS No. 141R also provides disclosure requirements related to business combinations. SFAS No. 141R is effective for fiscal years beginning after December 15, 2008, which is our fiscal year 2010 that begins May 3, 2009. SFAS No. 141R will be applied





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## METHODE ELECTRONICS, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in thousands, except share data)

**2. RECENT ACCOUNTING PRONCEMENTS** Continued

prospectively to business combinations with an acquisition date on or after the effective date. This statement will generally affect acquisitions occurring after the adoption date.

In December 2007, the FASB issued SFAS No. 160, *Non-Controlling Interests in Consolidated Financial Statements* an amendment of ARB No. 51 ( SFAS No. 160 ). SFAS No. 160 establishes new standards for the accounting for and reporting of non-controlling interests (formerly minority interests) and for the loss of control of partially owned and consolidated subsidiaries. SFAS No. 160 does not change the criteria for consolidating a partially owned entity. SFAS No. 160 is effective for fiscal years beginning after December 15, 2008, which is our fiscal year 2010 that begins May 3, 2009. The provisions of SFAS No. 160 will be applied prospectively upon adoption except for the presentation and disclosure requirements, which will be applied retrospectively. We do not expect the adoption of SFAS No. 160 to have a material impact on our condensed consolidated financial statements.

In March 2008, the FASB issued SFAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities*, an amendment of SFAS No. 133 ( SFAS No. 161 ). SFAS No. 161 requires enhanced disclosures about an entity's derivative and hedging activities and is effective for fiscal years and interim periods beginning after November 15, 2008, which is our fiscal year 2010 that begins May 3, 2009. We do not believe the adoption of SFAS No. 161 will have a material impact our condensed consolidated financial statements.

**3. RESTRUCTURING**

On January 24, 2008, we announced a restructuring of our U.S.-based automotive operations and a decision to discontinue producing certain legacy products in the Interconnect segment. The Automotive and Interconnect restructuring is expected to be completed by the end of the fourth quarter of fiscal year 2009. We record the expense in the restructuring section of our condensed consolidated statement of income. We estimate that we will record additional pre-tax charges during the rest of fiscal year 2009 of between \$10,000 and \$15,000, of which \$2,000 to \$5,000 will relate to the termination of approximately 650 employees and the cost of one-time employee benefits, retention, COBRA and outplacement services. We will continue to perform periodic impairment testing, if indicators exist, and will record any charges incurred as per SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* in the period when impairment is incurred.

During the fiscal quarter ended August 2, 2008, we recorded a restructuring charge of \$4,917, which consisted of \$2,821 for employee severance, \$1,550 in accelerated depreciation for buildings and improvements and machinery and equipment, \$154 in inventory write-down and \$392 relating to professional fees. As of August 2, 2008, we had an accrued restructuring liability of \$4,417 reflected in the current liabilities section of our condensed consolidated balance sheet. We expect this liability to be paid out by the end of the fourth quarter of fiscal year 2009. The table below reflects the activity for restructuring as of August 2, 2008:

|   | <b>One-Time<br/>Employee<br/>Benefits</b> | <b>Asset<br/>Write-Downs</b> | <b>Other<br/>Costs</b> | <b>Total</b> |
|---|---|------------------------------|------------------------|--------------|
| FY 2008 restructuring charges               | \$ 3,355                                  | \$ 1,346                     | \$ 458                 | \$ 5,159     |
| Payments and asset write-downs              | (203)                                     | (1,346)                      | (434)                  | (1,983)      |
| Accrued balance at May 3, 2008              | 3,152                                     |                              | 24                     | 3,176        |
| First Quarter FY 2009 restructuring charges | 2,821                                     | 1,703                        | 393                    | 4,917        |
| Payments and asset write-downs              | (1,556)                                   | (1,703)                      | (417)                  | (3,676)      |
| Accrued balance at August 2, 2008           | 4,417                                     |                              |                        | 4,417        |



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## METHODE ELECTRONICS, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in thousands, except share data)

## 4. COMPREHENSIVE INCOME

The components of our comprehensive income for the three months ended August 2, 2008 and July 28, 2007 include net income and adjustments to stockholders' equity for foreign currency translations. The foreign currency translation adjustment was due to exchange rate fluctuations in our foreign affiliates' local currency versus the U.S. dollar.

The following table presents details of our comprehensive income:

|                            | Three Months Ended |               |
|----------------------------|--------------------|---------------|
|                            | August             | July 28, 2007 |
|                            | 2,                 |               |
|                            | 2008               | 2007          |
| Net income                 | \$ 6,816           | \$ 8,272      |
| Translation adjustment     | 1,735              | (248)         |
| Total comprehensive income | \$ 8,551           | \$ 8,024      |

## 5. GOODWILL AND INTANGIBLE ASSETS

In connection with the Power Products segment's acquisition of Cableco Technologies in fiscal 2005, additional contingent consideration may be due if certain operational and financial targets are met. Additional goodwill of up to \$4,257 may result from future contingent payments for this acquisition.

On August 31, 2007, we acquired 100% of the assets of Value Engineered Products, Inc. (VEP) for \$5,750 in cash, plus transaction costs of \$79. VEP is a thermal management solutions provider, manufacturing heat sinks and related products for high-powered applications. These components complement our Power Products product offerings and, in some instances, are joined with bus bars to aid thermal management of power systems. The terms of the acquisition provide for an additional payment of up to a maximum of \$1,000 if sales reach specified targets during the twelve-month period following the close. Based on preliminary estimates, we anticipate the additional payout will be approximately \$750.

Based on a third-party valuation report, we estimate the tangible net assets acquired in the VEP transaction had a fair value of \$915. The fair values assigned to intangible assets acquired were \$2,900 for customer relationships, \$600 for trademarks, resulting in \$1,414 of goodwill. The customer relationships acquired are being amortized over a period of approximately 16 years, which began in September 2007. The trademark intangible assets are not subject to amortization but will be subject to periodic impairment testing. The accounts and transactions of the acquired business have been included in the Power Products segment in the consolidated financial statements from the effective date of the acquisition.

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METHODE ELECTRONICS, INC. AND SUBSIDIARIES  
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)  
 (Dollar amounts in thousands, except share data)

## 5. GOODWILL AND INTANGIBLE ASSETS Continued

The following tables present details of the Company's intangible assets:

|                                       | Gross            | August 2, 2008           |                  |
|---------------------------------------|------------------|--------------------------|------------------|
|                                       |                  | Accumulated Amortization | Net              |
| Customer relationships and agreements | \$ 41,299        | \$ 20,137                | \$ 21,162        |
| Patents and technology licenses       | 24,799           | 6,124                    | 18,675           |
| Covenants not to compete              | 2,480            | 2,271                    | 209              |
| <b>Total</b>                          | <b>\$ 68,578</b> | <b>\$ 28,532</b>         | <b>\$ 40,046</b> |

|                                       | Gross            | May 3, 2008              |                  |
|---------------------------------------|------------------|--------------------------|------------------|
|                                       |                  | Accumulated Amortization | Net              |
| Customer relationships and agreements | \$ 41,324        | \$ 19,168                | \$ 22,156        |
| Patents and technology licenses       | 24,692           | 5,795                    | 18,897           |
| Covenants not to compete              | 2,480            | 2,251                    | 229              |
| <b>Total</b>                          | <b>\$ 68,496</b> | <b>\$ 27,214</b>         | <b>\$ 41,282</b> |

The intangible assets for customer relationships and agreements includes \$2,059 and \$2,278 as of August 2, 2008 and May 3, 2008, respectively, of net value assigned to a supply agreement with Delphi Corporation, acquired in our acquisition of the passive occupancy detection systems (PODS) business in August 2001. Delphi is currently operating under a bankruptcy petition filed on October 8, 2005. We continue to supply product to Delphi post-petition pursuant to this supply agreement and have determined that the value of the supply agreement has not been impaired.

The estimated aggregate amortization expense for fiscal 2009 and each of the four succeeding fiscal years is as follows:

|      |         |
|------|---------|
| 2009 | \$5,169 |
| 2010 | 4,996   |
| 2011 | 4,865   |
| 2012 | 3,941   |
| 2013 | 3,176   |

## 6. INCOME TAXES

We recognize interest and penalties accrued related to the unrecognized tax benefits in the provision for income taxes. During the three months ended August 2, 2008, we recognized \$75 in interest and zero in penalties. We had approximately \$859 for the payment of interest and zero for the payment of penalties accrued at August 2, 2008. The total unrecognized tax benefits as of August 2, 2008 was \$5,770.

We believe that it is reasonably possible that the total amount of unrecognized tax benefits will change within the next twelve months. We have certain tax return years subject to statutes of limitation, which will close within twelve months of the end of the quarter. Unless challenged by tax authorities, the closure of those statutes of limitation is expected to result in the recognition of uncertain tax positions in the amount of \$491.

The Company and all of its domestic subsidiaries file income tax returns in the U.S. federal jurisdiction and various states. Our foreign subsidiaries file income tax returns in certain foreign jurisdictions since they have operations

outside the U.S. The Company and its subsidiaries are generally no longer subject to U.S. federal, state and local examinations by tax authorities for years before fiscal year 2005.

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METHODE ELECTRONICS, INC. AND SUBSIDIARIES  
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)  
 (Dollar amounts in thousands, except share data)

**7. COMMON STOCK AND STOCK-BASED COMPENSATION**

The following table sets forth the changes in the number of issued shares of common stock during the three month periods presented:

|  | Three Months Ended |                  |
|--|--------------------|------------------|
|  | August 2,<br>2008  | July 28,<br>2007 |
| Balance at the beginning of the period | 38,225,379         | 37,950,829       |
| Options exercised                      | 18,189             | 87,149           |
| Restricted stock awards vested         | 38,397             |                  |
| Balance at the end of the period       | 38,281,965         | 38,037,978       |

We paid a quarterly dividend of \$1,895 on August 2, 2008. We intend to retain the remainder of our earnings not used for dividend payments to provide funds for the operation and expansion of our business.

The following tables summarize the stock option activity and related information for the three months ended August 2, 2008:

|                               | Summary of Option Activity |                                |
|-------------------------------|----------------------------|--------------------------------|
|                               | Shares                     | Wtd. Avg.<br>Exercise<br>Price |
| Outstanding at May 3, 2008    | 689,689                    | \$ 10.26                       |
| Exercised                     | (18,189)                   | 5.72                           |
| Forfeited                     | (16,821)                   | 11.57                          |
| Outstanding at August 2, 2008 | 654,679                    | 10.35                          |

Options Outstanding and  
 Exercisable at August 2, 2008

| Range of          | Shares  | Wtd.<br>Avg.<br>Exercise<br>Price | Avg.<br>Remaining<br>Life<br>(Years) |
|-------------------|---------|-----------------------------------|--------------------------------------|
| Exercise Prices   |         |                                   |                                      |
| \$5.12 - \$7.69   | 161,025 | \$ 6.71                           | 2.8                                  |
| \$8.08 - \$11.64  | 353,305 | 10.58                             | 2.6                                  |
| \$12.11 - \$17.66 | 140,349 | 13.94                             | 1.8                                  |
|                   | 654,679 | 10.35                             |                                      |

Prior to June 21, 2007, we had three active stock plans, the Methode Electronics, Inc. 1997 Stock Plan, the Methode Electronics, Inc. 2000 Stock Plan, and the Methode Electronics, Inc. 2004 Stock Plan. No options were granted under the Plans since the first quarter of fiscal 2005. As of August 2, 2008, we had 654,679 unexercised stock options, all of which are fully vested and have a term of ten years. There is no remaining unrecognized compensation expense relating to the stock options.

In April 2007, 225,000 shares of common stock subject to performance-based Restricted Stock Awards (RSAs) granted to our CEO in fiscal 2006 and 2007 were converted to Restricted Stock Units (RSUs). The RSUs are subject to the same vesting schedule and other major provisions of the RSAs they replaced, except the RSUs are not payable until the earlier of: (1) thirty days after the CEO's date of termination of employment with the Company and all of its subsidiaries and affiliates; or (2) the last day of our fiscal year in which the payment of common stock in satisfaction of the RSUs becomes deductible to the Company under Section 162(m) of the Internal Revenue Code. All further discussion of RSAs in this report includes the RSUs described above.



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METHODE ELECTRONICS, INC. AND SUBSIDIARIES  
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)  
 (Dollar amounts in thousands, except share data)

**7. COMMON STOCK AND STOCK-BASED COMPENSATION** Continued

At the beginning of fiscal year 2009, there were 582,298 performance-based and time-based RSAs outstanding. The time-based RSAs vest in three equal annual installments from the grant date. All RSAs awarded to senior management are performance-based and vest after three years if the recipient remains employed by the Company until that date and we have met certain revenue growth and return on invested capital targets. All of the unvested RSAs are entitled to voting rights and to payment of dividends. During the three months ended August 2, 2008, we awarded 340,665 restricted stock awards. Of the shares granted, 24,000 shares vest immediately upon grant, 256,565 are performance-based RSAs and 60,100 are time-based RSAs.

We recognized pre-tax compensation expense for RSAs of \$792 and \$425 in the three months ended August 2, 2008 and July 28, 2007, respectively. We record the expense in the selling and administrative section of our condensed consolidated statement of income.

The following table summarizes the RSA activity for the three months ended August 2, 2008:

|                            |          |
|----------------------------|----------|
|                            | Shares   |
| Unvested at May 3, 2008    | 582,298  |
| Awarded                    | 340,665  |
| Vested                     | (24,332) |
| Forfeited                  |          |
| Unvested at August 2, 2008 | 898,631  |

The table below shows the Company's unvested RSAs at August 2, 2008:

| Grant Fiscal Year | RSAs    | Vesting Period                   | Weighted Average Value | Probable Unearned Compensation Expense at August 2, 2008 | Target Unearned Compensation Expense at August 2, 2008 |
|-------------------|---------|----------------------------------|------------------------|--|--|
| 2006              | 832     | 3-year equal annual installments | 10.84                  |  |  |
| 2006              | 125,000 | 3-year cliff                     | 12.42                  |  |  |
| 2007              | 24,757  | 3-year equal annual installments | 7.87                   | 40   | 40   |
| 2007              | 227,750 | 3-year cliff                     | 7.79                   | 460  | 460  |
| 2008              | 38,954  | 3-year equal annual installments | 14.97                  | 280  | 280  |
| 2008              | 164,673 | 3-year cliff                     | 15.14                  | 1,615  | 1,615  |
| 2009              | 60,100  | 3-year equal annual installments | 11.35                  | 626  | 626  |
| 2009              | 256,565 | 3-year cliff                     | 11.35                  | 2,747  | 2,747  |

At August 2, 2008, the aggregate unvested RSAs had a weighted average fair value of \$11.35 and a weighted average vesting period of approximately 19 months.

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## METHODE ELECTRONICS, INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in thousands, except share data)

## 8. EARNINGS PER SHARE

Basic earnings per share (EPS) is calculated by dividing net earnings by the weighted average number of common shares outstanding for the applicable period. Diluted EPS is calculated after adjusting the numerator and the denominator of the basic EPS calculation for the effect of all potential dilutive common shares outstanding during the period.

The following table sets forth the computation of basic and diluted earnings per share:

|  | Three Months Ended |               |
|--|--------------------|---------------|
|  | August 2,<br>2008  | July 28, 2007 |
| Numerator net income   | \$ 6,816           | \$ 8,272      |
| Denominator:   |                    |               |
| Denominator for basic earnings per share-weighted-average shares                                     | 37,198             | 36,993        |
| Dilutive potential common shares-employee stock options  | 446                | 498           |
| Denominator for diluted earnings per share adjusted weighted- average shares and assumed conversions | 37,644             | 37,491        |
| Basic and diluted net income per share:  |                    |               |
| Basic  | \$ 0.18            | \$ 0.22       |
| Diluted  | \$ 0.18            | \$ 0.22       |

Options to purchase 286,624 shares of common stock at a weighted-average exercise price of \$12.66 per share were outstanding as of August 2, 2008, but were not included in the computation of diluted earnings per share because the exercise prices were greater than the average market price of the common stock and, therefore, the effect would be antidilutive.

## 9. SEGMENT INFORMATION

We are a global manufacturer of component and subsystem devices. We design, manufacture and market devices employing electrical, electronic, wireless, sensing and optical technologies. Our components are found in the primary end markets of the automotive, appliance, communications (including information processing and storage, networking equipment, wireless and terrestrial voice/data systems), aerospace, rail and other transportation industries; and the consumer and industrial equipment markets.

We report in four operating segments Automotive, Interconnect, Power Products and Other. The Company's systems are not designed to capture information by smaller product groups and it would be impracticable to breakdown the Company's sales into smaller product groups.

On January 24, 2008, we announced a restructuring of our U.S.-based automotive operations and a decision to discontinue producing certain legacy products in the Interconnect segment. During the three months ended August 2, 2008, we recorded a restructuring charge of \$3,215 and \$1,702 for the Automotive and Interconnect segments, respectively.

The Automotive segment supplies electronic and electromechanical devices and related products to automobile OEMs, either directly or through their tiered suppliers, including control switches for electrical power and signals, connectors for electrical devices, integrated control components, switches and sensors that monitor the operation or status of a component or system, and packaging of electrical components.

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METHODE ELECTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

(Dollar amounts in thousands, except share data)

9. SEGMENT INFORMATION Continued

The Interconnect segment provides a variety of copper and fiber-optic interconnect and interface solutions for the appliance, computer, networking, telecommunications, storage, medical, military, aerospace, commercial and consumer markets. Solutions include solid-state field effect interface panels, PC and express card packaging, optical and copper transceivers, terminators, connectors, custom cable assemblies and conductive polymer and thick film inks. Services include the design and installation of fiber optic and copper infrastructure systems, and manufacturing of active and passive optical components.

In fiscal 2008, we changed the name of our power segment from Power Distribution to Power Products to more clearly reflect the activities of the segment. The Power Products segment manufactures current-carrying laminated bus devices, custom power-product assemblies; powder coated bus bars, braided flexible cables and high-current low voltage flexible power cabling systems that are used in various markets and applications, including telecommunications, computers, transportation, industrial and power conversion, insulated gate bipolar transistor solutions, aerospace and military.

The Other segment includes a designer and manufacturer of magnetic torque sensing products, and independent laboratories that provide services for qualification testing and certification, and analysis of electronic and optical components.

The accounting policies of the segments are the same as those described in the summary of significant accounting policies. We allocate resources to and evaluate performance of segments based on operating income. Transfers between segments are recorded using internal transfer prices set by us.

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METHODE ELECTRONICS, INC. AND SUBSIDIARIES  
 NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)  
 (Dollar amounts in thousands, except share data)

## 9. SEGMENT INFORMATION Continued

The table below presents information about our reportable segments:

|   | Three Months Ended August 2, 2008 |                   |                   |          |                   | Consoli-<br>dated |
|---|-----------------------------------|-------------------|-------------------|----------|-------------------|-------------------|
|   | Auto-<br>motive                   | Inter-<br>Connect | Power<br>Products | Other    | Elimi-<br>nations |                   |
| Net sales   | \$ 84,733                         | \$ 35,718         | \$ 12,135         | \$ 2,223 | \$ 295            | \$ 134,514        |
| Transfers between segments                              |                                   | (132)             | (134)             | (29)     | (295)             |                   |
| Net sales to unaffiliated<br>customers                  | \$ 84,733                         | \$ 35,586         | \$ 12,001         | \$ 2,194 | \$                | \$ 134,514        |
| Segment income (loss)<br>before restructuring charge    | \$ 13,650                         | \$ 2,123          | \$ 802            | \$ (582) | \$                | \$ 15,993         |
| Restructuring   | (3,215)                           | (1,702)           |                   |          |                   | (4,917)           |
| Segment income (loss)<br>including restructuring charge | \$ 10,435                         | \$ 421            | \$ 802            | \$ (582) | \$                | \$ 11,076         |
| Corporate expenses, net                                 |                                   |                   |                   |          |                   | (2,363)           |
| Income before income taxes                              |                                   |                   |                   |          |                   | \$ 8,713          |

|   | Three Months Ended July 28, 2007 |                   |                   |          |                   | Consoli-<br>dated |
|---|----------------------------------|-------------------|-------------------|----------|-------------------|-------------------|
|   | Auto-<br>motive                  | Inter-<br>Connect | Power<br>Products | Other    | Elimi-<br>nations |                   |
| Net sales   | \$ 82,862                        | \$ 31,586         | \$ 9,335          | \$ 1,674 | \$ 448            | \$ 125,009        |
| Transfers between segments                              |                                  | (178)             | (256)             | (14)     | (448)             |                   |
| Net sales to unaffiliated<br>customers                  | \$ 82,862                        | \$ 31,408         | \$ 9,079          | \$ 1,660 | \$                | \$ 125,009        |
| Segment income (loss)<br>before restructuring charge    | \$ 11,741                        | \$ 2,401          | \$ 1,849          | \$ (275) | \$                | \$ 15,716         |
| Restructuring   |                                  |                   |                   |          |                   |                   |
| Segment income (loss)<br>including restructuring charge | \$ 11,741                        | \$ 2,401          | \$ 1,849          | \$ (275) | \$                | \$ 15,716         |
| Corporate expenses, net                                 |                                  |                   |                   |          |                   | (4,644)           |

Income before income taxes

\$ 11,072

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**METHODE ELECTRONICS, INC. AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)**

(Dollar amounts in thousands, except share data)

**10. CONTINGENCIES**

Certain litigation arising in the normal course of business is pending against us. We are from time to time subject to various legal actions and claims incidental to our business, including those arising out of alleged defects, breach of contracts, employment-related matters and environmental matters. We consider insurance coverage and third-party indemnification when determining required accruals for pending litigation and claims. Although the outcome of potential legal actions and claims cannot be determined, it is our opinion, based on the information available, that we have adequate reserves for these liabilities and that the ultimate resolution of these matters will not have a material effect on our consolidated financial statements.

**11. PRE-PRODUCTION COSTS RELATED TO LONG-TERM SUPPLY ARRANGEMENTS**

We incur pre-production tooling costs related to certain products produced for our customers under long-term supply agreements. We had \$7,859 and \$8,211 as of fiscal periods ended August 2, 2008 and May 3, 2008, respectively, of pre-production tooling costs related to customer-owned tools for which reimbursement is contractually guaranteed by the customer or for which the customer has provided a non-cancelable right to use the tooling. These amounts are included in our work-in-process inventory in the condensed consolidated balance sheets. Net revenues and costs on projects are deferred and recognized over the life of the related long-term supply agreement.

**12. FAIR VALUE MEASUREMENTS**

We adopted SFAS No. 157, Fair Value Measurements as of May 4, 2008. SFAS No. 157 defines fair value 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.

In February 2008, the FASB issued FASB Staff Position No. 157-2, which delays the effective date of SFAS No. 157 for non-financial assets and liabilities, which are not measured at fair value on a recurring basis (at least annually) until fiscal years beginning after November 15, 2008, which is our fiscal year 2010 that begins May 3, 2009. We are currently assessing the impact of adopting SFAS No. 157 for non-financial assets and liabilities on our condensed consolidated financial statements.

SFAS No. 157 also specifies a fair value hierarchy based upon the observation of inputs in valuation techniques. Observable inputs (highest level) reflect market data obtained from independent sources, while unobservable inputs (lowest level) reflect internally developed market assumptions. In accordance with SFAS No. 157, fair value measurements are classified under the following hierarchy:

Level 1 Quoted prices in active markets for identical assets and liabilities.

Level 2 Quoted prices in active markets for similar assets and liabilities, or other inputs that are observable for the asset or liability, either directly or indirectly, for substantially the full term of the financial instrument.

Level 3 Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets and liabilities. This includes certain pricing models, discounted cash flow methodologies and similar techniques that use significant unobservable inputs.

The adoption of SFAS No. 157 had no effect on our condensed consolidated financial position or results of operations. Assets and liabilities recorded at fair value are valued using quoted market prices or under a market approach using other relevant information generated by market transactions involving identical or comparable instruments and included:

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## 12. FAIR VALUE MEASUREMENTS Continued

|  | Recorded<br>Value | Fair value measurement used   |   |  |
|--|-------------------|---|---|--|
|  |                   | Quoted<br>prices<br>in active<br>markets for<br>identical<br>instruments<br>(Level 1) | Quoted<br>prices<br>in active<br>markets for<br>similar<br>instruments<br>(Level 2) | Other<br>unobservable<br>inputs<br>(Level 3) |
| Assets:                                      |                   |   |   |  |
| Cash and Cash Equivalents (1)                | \$ 111,488        | \$ 111,488  | \$  | \$   |
| Assets Related to Deferred Compensation Plan | \$ 2,122          | \$  | \$ 2,122  | \$   |
| Total Assets at Fair Value                   | \$ 113,610        | \$ 111,488  | \$ 2,122  | \$   |
| Liabilities:                                 |                   |   |   |  |
| Deferred Compensation Plan                   | \$ 2,046          | \$ 2,046  | \$  | \$   |
| Total Liabilities at Fair Value              | \$ 2,046          | \$ 2,046  | \$  | \$   |

(1) Includes cash, money-market investments and certificates of deposit.

## Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

**Cautionary Statement**

Certain statements in this report are forward-looking statements that are subject to certain risks and uncertainties. We undertake no duty to update any such forward-looking statements to conform to actual results or changes in our expectations. Our business is highly dependent upon two large automotive customers and specific makes and models of automobiles. Our results will be subject to many of the same risks that apply to the automotive, appliance, computer and telecommunications industries, such as general economic conditions, interest rates, consumer spending patterns and technological changes. Other factors, which may result in materially different results for future periods, include the following risk factors. These risk factors should be considered in connection with evaluating the forward-looking statements contained in this report because these factors could cause our actual results and condition to differ materially from those projected in forward-looking statements. The forward-looking statements in this report are subject to the safe harbor protection provided under the securities laws.

We depend on a small number of large customers. If we were to lose any of these customers or any of these customers decreased the number of orders it placed, our future results could be adversely affected.

Because we derive approximately 63% of our revenues from the automotive segment, rising oil prices could adversely affect future results.

Our business is cyclical and seasonal in nature and further downturns in the automotive industry could reduce the sales and profitability of our business.

Because we derive approximately 63% of our revenues from the automotive industry, any downturns or challenges faced by this industry may have an adverse effect on our business, financial condition and operating results.





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***Cautionary Statement Continued***

Because we derive a substantial portion of our revenues from customers in the automotive, appliance, computer and communications industries, we are susceptible to trends and factors affecting those industries.

We are subject to intense pricing pressures in the automotive industry.

We are dependent on the availability and price of raw materials.

We face risks relating to our international operations.

Our technology-based business and the markets in which we operate are highly competitive. If we are unable to compete effectively, our sales will decline.

If we are unable to protect our intellectual property or we infringe, or are alleged to infringe, on another person's intellectual property, our business, financial condition and operating results could be materially adversely affected.

We may be unable to keep pace with rapid technological changes, which would adversely affect our business.

Products we manufacture may contain design or manufacturing defects that could result in reduced demand for our products or services and liability claims against us.

We may acquire businesses or divest of various business operations. These transactions may pose significant risks and may materially adversely affect our business, financial condition and operating results.

Any such forward-looking statements are not guarantees of future performance and actual results, developments and business decisions may differ materially from those foreseen in such forward-looking statements. These forward-looking statements speak only as of the date of the report, press release, statement, document, webcast or oral discussion in which they are made. We do not intend to update any forward-looking statement, all of which are expressly qualified by the foregoing. See Part I Item A, Risk Factors of our latest Form 10-K for the fiscal year ended May 3, 2008, for a further discussion regarding some of the reasons that actual results may be materially different from those we anticipate.

***Overview***

We are a global manufacturer of component and subsystem devices with manufacturing, design and testing facilities in the United States, Malta, Mexico, United Kingdom, Germany, Czech Republic, China, India and Singapore. We design, manufacture and market devices employing electrical, electronic, wireless, sensing and optical technologies. Our business is managed on a segment basis, with those segments being Automotive, Interconnect, Power Products and Other. For more information regarding the business and products of these segments, see Item 1. Business of our Form 10-K for the fiscal year ended May 3, 2008.

Our components are found in the primary end markets of the automotive, information processing and networking equipment, voice and data communication systems, consumer electronics, appliance, aerospace vehicles and industrial equipment industries. Our products employ electronic and optical technologies to control and convey signals through sensors, interconnections and controls. Recent trends in the industries that we serve include:

continued customer migration to lower-cost Eastern European and Asian suppliers;

growth of North American subsidiaries of foreign-based automobile manufacturers;

rising raw material costs;

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***Overview Continued***

the deteriorating financial condition of certain of our customers and the uncertainty as they undergo restructuring initiatives, including in some cases, reorganization under bankruptcy laws;

increasing pressure by automobile manufacturers on automotive suppliers to reduce selling prices;

more supplier-funded design, engineering and tooling costs previously funded by the automobile manufacturers;

reduced production schedules for domestic automobile manufacturers; and rising interest rates.

decline in demand for less fuel-efficient trucks and SUVs.

On August 31, 2007, we acquired 100% of the assets of Value Engineered Products, Inc. (VEP) for \$5.8 million in cash. VEP is a thermal management solutions provider, manufacturing heat sinks and related products for high-powered applications. These components complement our Power Product offerings and, in some instances, are joined with bus bars to aid thermal management of power systems.

On March 30, 2008, we acquired 100% of the assets of Tribotek, Inc for \$1.8 million in cash. Tribotek designs, develops and manufactures high current power connectors and power product systems for products such as power supplies, servers, rectifiers, inverters, robotics and automated test equipment, in addition to various military and telecommunication applications.

In response to pricing pressures, we continue to employ lean manufacturing processes, invest in and implement techniques to lower our costs in order to reduce or prevent margin erosion. We also have become more selective with regard to programs, in which we participate in order to reduce our exposure to lower-profit programs, and have transferred several automotive manufacturing lines, and identified additional lines to be transferred, from the U.S. to lower-cost countries.

On January 24, 2008, we announced a restructuring of our U.S.-based automotive operations and a decision to discontinue producing certain legacy electronic Interconnect products. The Automotive and Interconnect restructuring is expected to be completed by the end of the fourth quarter of fiscal year 2009. During the fiscal quarter ended August 2, 2008, we recorded a restructuring charge of \$4,917, which consisted of \$2,821 for employee severance, \$1,550 in accelerated depreciation for buildings and improvements and machinery and equipment, \$154 for inventory write-down and \$392 relating to professional fees. We record the expense in the restructuring section of our consolidated statement of income. We estimate that we will record additional pre-tax charges during the rest of fiscal 2009 of between \$10,000 and \$15,000, of which \$2,000 to \$5,000 will relate to the termination of approximately 650 employees and the cost of one-time employee benefits, retention, COBRA and outplacement services. We will continue to perform periodic impairment testing and will record any charges incurred as per FASB 144, *Accounting for the Impairment or Disposal of Long-Lived Assets* in the period when impairment is incurred.

**Business Outlook**

Sales in fiscal 2009 are expected to decrease compared to fiscal 2008. Sales of Automotive segment products are expected to decline, as forecasted sales from North American automotive OEMs are lower and demand for less fuel-efficient trucks and sports utility vehicles continues to decline. We expect to significantly reduce sales to Chrysler due to our decision to discontinue manufacturing their unprofitable and marginally profitable legacy products. Sales of sensor pads for passive occupant-detection systems are expected to decline due to the lower North American automotive volumes. We expect growth in the Interconnect segment as increased sales of field-effect and optical products will offset lower sales of legacy Interconnect products related to our decision to exit this business. We also expect growth in our Power Products segment as we begin to benefit from the synergies related to the VEP and Tribotek acquisitions. In addition, our Power Products segment plans to expand geographically into Northern Africa. We expect this will enable the Power Products segment to further penetrate the European market. As the Interconnect segment transitions away from lower margin legacy products, new products, such as, field-effect user-interface panels, are expected to penetrate industrial, automotive and other transportation markets. These products are also being introduced into the European appliance market. Margins are expected to decrease in fiscal 2009 due to increasing

material costs, customer pressure to reduce selling prices and weaker automotive sales. Margins in fiscal 2008 significantly benefited from price increases received from Chrysler on their legacy business.

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The benefit of those price increases is expected to decrease significantly in fiscal 2009 as Chrysler is expected to complete the transition of their business to other suppliers.

**Results of Operations for the Three Months Ended August 2, 2008 as Compared to the Three Months Ended July 28, 2007****Consolidated Results**

Below is a table summarizing results for the three months ended:  
(in millions)

|  | August<br>2,<br>2008 | July 28,<br>2007 | Net<br>Change | Net<br>Change |
|--|----------------------|------------------|---------------|---------------|
| Net sales                              | \$ 134.5             | \$ 125.0         | \$ 9.5        | 7.6%          |
| Other income                           | 0.7                  | 0.2              | 0.5           | 250.0%        |
|  | 135.2                | 125.2            | 10.0          | 8.0%          |
| Cost of products sold                  | 105.4                | 98.3             | 7.1           | 7.2%          |
| Gross margins (including other income) | 29.8                 | 26.9             | 2.9           | 10.8%         |
| Restructuring                          | 4.9                  |                  | 4.9           | 0.0%          |
| Selling and administrative expenses    | 16.5                 | 16.0             | 0.5           | 3.1%          |
| Interest income, net                   | 0.5                  | 0.4              | 0.1           | 25.0%         |
| Other, net                             | (0.2)                | (0.2)            |               | 0.0%          |
| Income taxes                           | 1.9                  | 2.8              | (0.9)         | -32.1%        |
| Net income                             | \$ 6.8               | \$ 8.3           | \$ (1.5)      | -18.1%        |

|  | August<br>2,<br>2008 | July 28,<br>2007 |
|--|----------------------|------------------|
| Percent of sales:                      |                      |                  |
| Net sales                              | 100.0%               | 100.0%           |
| Other income                           | 0.5%                 | 0.2%             |
| Cost of products sold                  | 78.4%                | 78.6%            |
| Gross margins (including other income) | 22.2%                | 21.5%            |
| Restructuring                          | 3.6%                 | 0.0%             |
| Selling and administrative expenses    | 12.3%                | 12.8%            |
| Interest income, net                   | 0.4%                 | 0.3%             |
| Other, net                             | -0.1%                | -0.2%            |
| Income taxes                           | 1.4%                 | 2.2%             |
| Net income                             | 5.1%                 | 6.6%             |

*Net Sales.* Consolidated net sales increased \$9.5 million, or 7.6%, to \$134.5 million for the three months ended August 2, 2008 from \$125.0 million for three months ended July 28, 2007. The increase primarily is due to strong sales from our Asian Interconnect businesses and the Interconnect segment's Touchsensor business as well as strong sales from our Asian Power Products business. North American Automotive segment sales were favorably impacted by year over year net price increases of \$3.9 million on what was previously marginally profitable and unprofitable products, which we had decided to exit at the expiration of our manufacturing commitment but, at the request of the customer, have agreed to continue to produce at higher prices. The North American net sales (including the price increases) were partially offset by weaker sales from our Asian automotive business. Translation of foreign operations net sales in the three months ended August 2, 2008 increased reported net sales by \$3.9 million or 3.1% due to currency rate fluctuations.

**Table of Contents****Consolidated Results Continued**

*Other Income.* Other income increased \$0.5 million, or 250.0%, to \$0.7 million for the three months ended August 2, 2008 from \$0.2 million for three months ended July 28, 2007. Other income consisted primarily of earnings from engineering design fees and royalties.

*Cost of Products Sold.* Consolidated cost of products sold increased \$7.1 million, or 7.2%, to \$105.4 million for the three months ended August 2, 2008 from \$98.3 million for the three months ended July 28, 2007. The increase is due to the higher sales volumes. Consolidated cost of products sold as a percentage of sales was 78.4% for the three months ended August 2, 2008 and 78.6% for the three months ended July 28, 2007. The Automotive segment cost of products sold as a percentage of sales were favorably impacted by price increases during the first quarter of fiscal 2009.

*Gross Margins (including other income).* Consolidated gross margins (including other income) increased \$2.9 million, or 10.8%, to \$29.8 million for the three months ended August 2, 2008 as compared to \$26.9 million for the three months ended July 28, 2007. Gross margins as a percentage of net sales was 22.2% for the three months ended August 2, 2008 as compared to 21.5% for the three months ended July 28, 2007. The increase in gross margin as a percentage of sales is due to the Automotive segment price increases during the first quarter of fiscal 2009.

*Selling and Administrative Expenses.* Selling and administrative expenses increased \$0.5 million, or 3.1%, to \$16.5 million for the three months ended August 2, 2008 compared to \$16.0 million for the three months ended July 28, 2007. The increase relates to higher stock award amortization expense of \$0.4 million and higher amortization expense related to intangible assets. Selling and administrative expenses as a percentage of net sales decreased to 12.3% in the three months ended August 2, 2008 from 12.8% for the three months ended July 28, 2007.

*Restructuring and Impairment Costs.* On January 24, 2008, we announced a restructuring of our U.S.-based automotive operations and the decision to discontinue producing certain legacy products in the Interconnect segment. During the fiscal quarter ended August 2, 2008, we recorded a restructuring charge of \$4.9 million (\$3.3 million after tax), which consisted of \$2.8 million for employee severance, \$1.6 million for accelerated depreciation for buildings and improvements and machinery and equipment, \$0.1 million for inventory write-down and \$0.4 relating to professional fees.

*Interest Income, Net.* Net interest income increased 25.0% in the three months ended August 2, 2008 to \$0.5 million as compared to \$0.4 million in the three months ended July 28, 2007. The average cash balance was \$116.0 million during the three months ended August 2, 2008 as compared to \$67.6 million during the three months ended July 28, 2007. The average interest rate earned in the three months ended August 2, 2008 was 1.98% compared to 3.02% in the three months ended July 28, 2007. The portfolio was weighted more heavily to tax-exempt investments in the first quarter of fiscal 2009 as compared to the first quarter of fiscal 2008. The average interest rate earned includes both taxable interest and tax-exempt municipal interest. Interest expense was \$0.1 million for both periods.

*Other, Net.* Other, net was an expense of \$0.2 million for both the three months ended August 2, 2008 and July 28, 2007. Other, net consists primarily of currency exchange gains and losses at the Company's foreign operations. The functional currencies of these operations are the British pound, Chinese yuan, Czech koruna, Euro, Mexican peso and Singapore dollar. Some foreign operations have transactions denominated in currencies other than their functional currencies, primarily sales in U.S. dollars and Euros, creating exchange rate sensitivities.

*Income Taxes.* The effective income tax rate was 21.8% in the first quarter of fiscal 2009 compared with 25.3% in the first quarter of fiscal 2008. The effective tax rates for both fiscal 2009 and 2008 reflect utilization of foreign investment tax credits and the effect of lower tax rates on income of the Company's foreign earnings and a higher percentage of earnings at those foreign operations.

*Net Income.* Net income decreased \$1.5 million, or 18.1%, to \$6.8 million for the three months ended August 2, 2008 as compared to \$8.3 million for the three months ended July 28, 2007 due to the restructuring charges and higher selling and administrative expenses, partially offset by automotive segment price increases. Net income as a percentage of sales decreased to 5.1% for the three months ended August 2, 2008 as compared to 6.6% for the three months ended July 28, 2007.



**Table of Contents****Operating Segments****Automotive Segment Results**

Below is a table summarizing results for the three months ended:

(in millions)

|  | August<br>2,<br>2008 | July 28,<br>2007 | Net<br>Change | Net<br>Change |
|--|----------------------|------------------|---------------|---------------|
| Net sales                                    | \$ 84.7              | \$ 82.9          | \$ 1.8        | 2.2%          |
| Cost of products sold                        | 67.6                 | 66.5             | 1.1           | 1.7%          |
| Gross margins                                | 17.1                 | 16.4             | 0.7           | 4.3%          |
| Income before income taxes and restructuring | \$ 13.7              | \$ 11.7          | \$ 2.0        | 17.1%         |
| Restructuring                                | (3.2)                |                  | (3.2)         | 0.0%          |
| Income before income taxes                   | \$ 10.5              | \$ 11.7          | \$ (1.2)      | -10.3%        |

| Percent of sales:                               | August<br>2,<br>2008 | July 28,<br>2007 |
|---|----------------------|------------------|
| Net sales                                       | 100.0%               | 100.0%           |
| Cost of products sold                           | 79.8%                | 80.2%            |
| Gross margins                                   | 20.2%                | 19.8%            |
| Income before income<br>taxes and restructuring | 16.2%                | 14.1%            |
| Restructuring                                   | -3.8%                | 0.0%             |
| Income before income<br>taxes                   | 12.4%                | 14.1%            |

*Net Sales.* Automotive segment net sales increased \$1.8 million, or 2.2%, to \$84.7 million for the three months ended August 2, 2008 from \$82.9 million for the three months ended July 28, 2007. During the first quarter of fiscal 2009 as compared to the first quarter of fiscal 2008, net sales increased in our Malta operation by 7.6% (predominately due to currency fluctuations), net sales declined slightly in our North American operations by 0.4% and net sales declined by 15.5% in our Asian operations. The decline in our Asian operation is due to lower demand for parts and components included in less fuel-efficient trucks and SUVs. North American sales were favorably impacted by year over year net price increases of \$3.9 million on what was previously marginally profitable and unprofitable products, which we had decided to exit at the expiration of our manufacturing commitment but, at the request of the customer, have agreed to continue to produce at higher prices. We anticipate the exit of producing these products will be complete during the third or fourth quarter of fiscal 2009. Excluding the price increases, North American sales declined 8.7% during the first quarter of fiscal 2009 as compared to the first quarter of fiscal 2008 due to lower demand in the U.S. automotive market. Translation of foreign operations net sales in the three months ended August 2, 2008 increased reported net sales by \$3.5 million, or 4.2%, due to currency rate fluctuations.

*Cost of Products Sold.* Automotive segment cost of products sold increased \$1.1 million to \$67.6 million for the three months ended August 2, 2008 from \$66.5 for the three months ended July 28, 2007. The increase relates to higher sales volumes from our Malta operation. Automotive segment costs of products sold as a





**Table of Contents****Automotive Segment Results Continued**

percentage of sales decreased to 79.8% for the three months ended August 2, 2008 from 80.2% for the three months ended July 28, 2007. Automotive segment cost of products sold as a percentage of sales was favorably impacted by price increases and the higher sales from our Malta operation which has a lower cost of products sold as a percentage of sales as compared to our North American operations.

*Gross Margins.* Automotive segment gross margins increased \$0.7 million, or 4.3%, to \$17.1 million for the three months ended August 2, 2008 as compared to \$16.4 million for the three months ended July 28, 2007. Gross margins as a percentage of net sales increased to 20.2% for the three months ended August 2, 2008 from 19.8% for the three months ended July 28, 2007. The increase in gross profit as a percentage of sales is primarily due to the pricing increases and higher sales from our Malta operation.

*Restructuring.* On January 24, 2008, we announced a restructuring of our U.S.-based automotive operations. During the fiscal quarter ended August 2, 2008, we recorded a restructuring charge of \$3.2 million, which consisted of \$2.2 million for employee severance, \$0.7 million for accelerated depreciation for buildings, building improvements and machinery and equipment and \$0.3 million for professional fees. We expect the restructuring to be completed by the fourth quarter of fiscal 2009.

*Income Before Income Taxes.* Automotive segment income before income taxes decreased \$1.2 million, or 10.3%, to \$10.5 million for the three months ended August 2, 2008 compared to \$11.7 million for the three months ended July 28, 2007 due to restructuring expenses, partially offset by the price increases and increased sales and income from our Malta operation.

**Interconnect Segment Results**

Below is a table summarizing results for the three months ended:

(in millions)

|  | August<br>2,<br>2008 | July 28,<br>2007 | Net<br>Change | Net<br>Change |
|--|----------------------|------------------|---------------|---------------|
| Net sales                                    | \$ 35.6              | \$ 31.4          | \$ 4.2        | 13.4%         |
| Cost of products sold                        | 26.6                 | 23.8             | 2.8           | 11.8%         |
| Gross margins                                | 9.0                  | 7.6              | 1.4           | 18.4%         |
| Income before income taxes and restructuring | \$ 2.2               | \$ 2.4           | \$ (0.2)      | -8.3%         |
| Restructuring                                | (1.7)                |                  | (1.7)         | 0.0%          |
| Income before income taxes                   | \$ 0.5               | \$ 2.4           | \$ (1.9)      | -79.2%        |

|   | August<br>2,<br>2008 | July 28,<br>2007 |
|---|----------------------|------------------|
| Percent of sales:                               |                      |                  |
| Net sales                                       | 100.0%               | 100.0%           |
| Cost of products sold                           | 74.7%                | 75.8%            |
| Gross margins                                   | 25.3%                | 24.2%            |
| Income before income<br>taxes and restructuring | 6.2%                 | 7.6%             |
| Restructuring                                   | -4.8%                | 0.0%             |

Income before income  
taxes

1.4%                      7.6%

*Net Sales.* Interconnect segment net sales increased \$4.2 million, or 13.4%, to \$35.6 million for the three months ended August 2, 2008 from \$31.4 million for the three months ended July 28, 2007. The net sales increase was driven by strong sales from our Asian connector business and our TouchSensor business. Translation of foreign operations net sales in the three months ended August 2, 2008 increased reported net sales by \$0.5 million, or 1.6%, due to currency rate fluctuations.

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*Cost of Products Sold.* Interconnect segment cost of products sold increased \$2.8 million to \$26.6 million for the three months ended August 2, 2008 compared to \$23.8 million for the three months ended July 28, 2007. The majority of the increase is due to higher net sales. Interconnect segment cost of products sold as a percentage of net sales decreased to 74.7% for the three months ended August 2, 2008 compared to 75.8% for the three months ended July 28, 2007. The decrease in cost of products sold as a percentage of net sales is due to higher net sales from our Shanghai, China operation which has a lower cost of products sold as a percentage of sales as compared to our North American operations.

*Gross Margins.* Interconnect segment gross margins increased \$1.4 million, or 18.4%, to \$9.0 million for the three months ended August 2, 2008 as compared to \$7.6 million for the three months ended July 28, 2007. The increase is due to higher sales and favorable costs from our Shanghai, China operation. Gross margins as a percentage of net sales increased to 25.3% for the three months ended August 2, 2008 from 24.2% for the three months ended July 28, 2007.

*Restructuring.* On January 24, 2008, we announced our decision to discontinue producing certain legacy products in the Interconnect segment. During the fiscal quarter ended August 2, 2008, we recorded a restructuring charge of \$1.7 million, which consisted of \$0.6 million for employee severance, \$0.9 million for accelerated depreciation for buildings, building improvements and machinery and equipment and \$0.2 for inventory write-downs. We expect the restructuring to be completed by the fourth quarter of fiscal 2009.

*Income Before Income Taxes.* Interconnect income before income taxes decreased \$1.9 million, or 79.2%, to \$0.5 million for the three months ended August 2, 2008 compared to \$2.4 million for the three months ended July 28, 2007 due to higher amortization expense, restructuring charges, partially offset by higher gross margins.

**Power Products Segment Results**

Below is a table summarizing results for the three months ended:

(in millions)

|                            | August<br>2,<br>2008 | July<br>28,<br>2007 | Net<br>Change | Net<br>Change |
|----------------------------|----------------------|---------------------|---------------|---------------|
| Net sales                  | \$ 12.0              | \$ 9.1              | \$ 2.9        | 31.9%         |
| Cost of products sold      | 9.7                  | 6.5                 | 3.2           | 49.2%         |
| Gross margins              | 2.3                  | 2.6                 | (0.3)         | -11.5%        |
| Income before income taxes | \$ 0.8               | \$ 1.8              | \$ (1.0)      | -55.6%        |

|                            | August<br>2,<br>2008 | July 28,<br>2007 |
|----------------------------|----------------------|------------------|
| Percent of sales:          |                      |                  |
| Net sales                  | 100.0%               | 100.0%           |
| Cost of products sold      | 80.8%                | 71.4%            |
| Gross margins              | 19.2%                | 28.6%            |
| Income before income taxes | 6.7%                 | 19.8%            |

*Net Sales.* Power Products segment net sales increased \$2.9 million to \$12.0 million for the three months ended August 2, 2008 from \$9.1 million for the three months ended July 28, 2007. Net sales increased due to the VEP acquisition and strong sales from our Asian busbar business. Excluding VEP, the Power Products segment sales increased 20.9% in the three months ended August 2, 2008.

**Table of Contents****Power Products Segment Results Continued**

*Cost of Products Sold.* Power Products segment cost of products sold increased \$3.2 million, or 49.2%, to \$9.7 million for the three months ended August 2, 2008 compared to \$6.5 million for the three months ended July 28, 2007. The Power Products segment cost of products sold as a percentage of sales increased to 80.8% for the three months ended August 2, 2008 from 71.4% for the three months ended July 28, 2007. The increase is partially due to a product which became end of life at the end of fiscal 2008 and had a lower cost as a percentage of sales than the remaining sales during the first quarter of fiscal 2009. In addition, we experienced material price increases in our busbar businesses, as well as, increased shipping and distribution costs.

*Gross Margins.* Power Products segment gross margins decreased \$0.3 million, or 11.5%, to \$2.3 million for the three months ended August 2, 2008 as compared to \$2.6 million for the three months ended July 28, 2007. Gross margins as a percentage of net sales decreased to 19.2% for the three months ended August 2, 2008 from 28.6% for the three months ended July 28, 2007. The decrease is due to a product which became end of life at the end of fiscal 2008 and had higher gross margins than the remaining sales and gross margins during the first quarter of fiscal 2009. We also experienced increased cost for material and labor as well as shipping and distribution costs.

*Income Before Income Taxes.* Power Products segment income before income taxes decreased by \$1.0 million or 55.6% to \$0.8 million for the three months ended August 2, 2008 from \$1.8 million for the three months ended July 28, 2007 due to decreased sales of products which became end of life at the end of fiscal year 2008, higher material, labor and shipping costs, higher commission expense and expenses related to Tribotek, which was acquired on March 30, 2008.

**Other Segment Results**

Below is a table summarizing results for the three months ended:

(in millions)

|                          | August<br>2,<br>2008 | July<br>28,<br>2007 | Net<br>Change | Net<br>Change |
|--------------------------|----------------------|---------------------|---------------|---------------|
| Net sales                | \$ 2.2               | \$ 1.7              | \$ 0.5        | 29.4%         |
| Cost of products sold    | 2.0                  | 1.5                 | 0.5           | 33.3%         |
| Gross margins            | 0.2                  | 0.2                 | 0.0           | 0.0%          |
| Loss before income taxes | \$ (0.6)             | \$ (0.3)            | \$ (0.3)      | 100.0%        |

|                          | August 2,<br>2008 | July 28,<br>2007 |
|--------------------------|-------------------|------------------|
| Percent of sales:        |                   |                  |
| Net sales                | 100.0%            | 100.0%           |
| Cost of products sold    | 90.9%             | 88.2%            |
| Gross margins            | 9.1%              | 11.8%            |
| Loss before income taxes | -27.3%            | -17.6%           |

*Net Sales.* The Other segment net sales increased \$0.5 million to \$2.2 million for the three months ended August 2, 2008 as compared to \$1.7 million for the three months ended July 28, 2007. Net sales from our torque-sensing business increased 229.0% and net sales from our testing facilities increased 11.2% in the first quarter of fiscal 2009 as compared to the first quarter of fiscal 2008.

*Cost of Products Sold.* Other segment cost of products sold increased \$0.5 million to \$2.0 million for the three months ended August 2, 2008 compared to \$1.5 million for the three months ended July 28, 2007. The majority of the increase is due to continued investment initiatives in our torque-sensing business.



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*Gross Margins.* The Other segment gross margins were \$0.2 million for both the three months ended August 2, 2008 and July 28, 2007. Gross margins were flat in the first quarter of fiscal 2009 due to the increased sales for both the torque-sensing business and the testing facilities, offset by increased investments in our torque-sensing business.

*Loss Before Income Taxes.* The Other segment loss before income taxes was \$0.6 million for the three months ended August 2, 2008 compared to \$0.3 million for the three months ended July 28, 2007. The increase in the loss before income taxes is due to additional support staff for our testing facilities in the first quarter of fiscal 2009.

**Liquidity and Capital Resources**

We have historically financed our cash requirements through cash flows from operations. We are currently pursuing opportunities to expand our business through acquisitions. If we are successful, our cash position will be reduced. Our future capital requirements will depend on a number of factors, including our future net sales and the timing and rate of expansion of our business. We believe our current cash balances together with the cash flow expected to be generated from future domestic and foreign operations will be sufficient to support current operations. We have an agreement with our primary bank for a committed \$75.0 million revolving credit facility to provide ready financing for general corporate purposes, including acquisition opportunities that may become available. The bank credit agreement, which expires on January 31, 2011, requires maintenance of certain financial ratios and a minimum net worth level. At August 2, 2008, the Company was in compliance with these covenants and there were no borrowings against this credit facility.

At August 2, 2008, approximately \$9.7 million was invested in an enhanced cash fund sold as an alternative to traditional money-market funds. We have historically invested a portion of our on hand cash balances in this fund. These investments are subject to credit, liquidity, market and interest rate risk. Based on the information available to us, we have estimated the fair value of this fund at \$0.965 per unit as of August 2, 2008. We recorded a two-thousand dollar loss on the net asset value (NAV) during the quarter. Subsequent to our August 2, 2008 first quarter-end and through September 11, 2008, the date of our first quarter fiscal year 2009 10-Q filing, we have received additional cash redemptions of \$1.9 million at \$0.964 per unit, leaving the new principal balance at \$7.8 million.

The latest information from fund management states that its goal is to have 83% of the portfolio liquidated by December 2008. Information and the markets relating to these investments remain dynamic, and there may be further declines in the value of these investments, the value of the collateral held by these entities, and the liquidity of our investments. To the extent we determine that there is a further decline in fair value, we may recognize additional losses in future periods.

Net cash provided by operating activities decreased \$8.3 million, or 42.3%, to \$11.3 million for the first three months of fiscal 2009 compared to \$19.6 million in the first three months of fiscal 2008. Our net income decreased \$1.5 million, or 18.1%, to \$6.8 million in the first three months of fiscal 2009 compared to \$8.3 million for the first three months of fiscal 2008. In the first quarter of fiscal 2008, we received a significant prepayment from a customer for products that were delivered during the fiscal year. The primary factor in the Company's ability to generate cash from operations is our net income. Additionally, cash flows from operations exceed net income because non-cash charges (depreciation, amortization of intangibles, restricted stock awards, and stock options) negatively impact net income but do not result in the use of cash. Similarly, non-cash credits such as deferred income tax benefits increase net income but do not provide cash. Additional contributors or offsets to cash flows from operations are working capital requirements.

Net cash used in investing activities during the first three months of fiscal 2009 was \$3.4 million compared to \$6.9 million for the first three months of fiscal 2008. Purchases of plant and equipment was \$3.3 million and \$4.7 million for the first three months of fiscal 2009 and 2008, respectively. In the first three months of fiscal 2008, we made additional payments of \$1.0 million relating to purchase price adjustments relating to the TouchSensor acquisition and a contingent payment of \$0.3 million related to the acquisition of Cableco Technologies. Additionally, a dividend payment of \$1.0 million was paid in the first three months of fiscal 2008 relating to our automotive joint venture.

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**Liquidity and Capital Resources Continued**

Net cash used in financing activities during the first three months in fiscal 2009 was \$1.7 million compared with \$0.7 million in the first three months of fiscal 2008. Proceeds from the exercise of stock options decreased \$1.0 million to \$0.1 million for the first three months of fiscal 2009 as compared to \$1.0 million in the first three months of fiscal 2008.

**Off-Balance Sheet Arrangements**

We do not have any off-balance sheet arrangements, other than operating leases and purchase obligations entered into in the normal course of business.

**Item 3. Quantitative And Qualitative Disclosures About Market Risk**

Certain of our foreign operations enter into transactions in currencies other than their functional currency, primarily the U.S. dollar and the Euro. A 10% change in foreign currency exchange rates from balance sheet date levels could impact our income before income taxes by \$1.1 million for both periods ended August 2, 2008 and May 3, 2008. We also have foreign currency exposure arising from the translation of our net equity investment in our foreign operations to U.S. dollars. We generally view our investments in foreign operations with functional currencies other than the U.S. dollar as long-term. The currencies to which we are exposed are the British pound, Chinese yuan, Czech koruna, Euro, Mexican peso and Singapore dollar. A 10% change in foreign currency exchange rates from balance sheet date levels could impact our net foreign investments by \$15.8 million at August 2, 2008 and \$15.1 million at May 3, 2008.

**Item 4. Controls And Procedures**

As of the end of the period covered by this quarterly report on Form 10-Q, we performed an evaluation under the supervision and with the participation of the Company's management, including our Chief Executive Officer and our Chief Financial Officer, of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934). The Company's disclosure controls and procedures are designed to ensure that the information required to be disclosed by the Company in the reports that we file or submit under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's applicable rules and forms. As a result of this evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were effective.

There have been no changes in our internal control over financial reporting during the quarter ended August 2, 2008 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.



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## PART II. OTHER INFORMATION

## Item 2. Unregistered Sales Of Equity Securities And Use Of Proceeds

## c) Purchase of equity securities by the issuer and affiliated purchasers.

| Period                              | Total<br>Number of<br>Shares<br>Purchased<br>(1) | Average<br>Price<br>Paid<br>Per<br>Share | Total Number<br>of<br>Shares<br>Purchased as<br>Part of<br>Publicly<br>Announced<br>Plans<br>or Programs | Maximum<br>Number of<br>Shares that<br>May Yet Be<br>Purchased<br>Under the Plans<br>or<br>Programs |
|-------------------------------------|--|--|--|---|
| May 4, 2008 through May 31, 2008    |  |  |  |   |
| June 1, 2008 through July 5, 2008   |  |  |  |   |
| July 6, 2008 through August 2, 2008 | 122  | \$ 11.54                                 |  |   |
|                                     | 122  | \$ 11.54                                 |  |   |

(1) The amount represents the repurchase and cancellation of shares of common stock redeemed by the Company for the payment of minimum withholding taxes on the value of restricted stock awards vesting during the period.

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Item 6. Exhibits

Exhibit

| Number | Description   |
|--------|---|
| 31.1   | Rule 13a-14(a)/15d-14(a) Certification of Principal Executive Officer         |
| 31.2   | Rule 13a-14(a)/15d-14(a) Certification of Principal Financial Officer         |
| 32     | Certification of Periodic Financial Report Pursuant to 18 U.S.C. Section 1350 |

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**SIGNATURES**

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

METHODE ELECTRONICS, INC.

By: */s/ Douglas A. Koman*  
Douglas A. Koman  
Chief Financial Officer  
(principal financial officer)

Dated: September 11, 2008

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INDEX TO EXHIBITS

| Exhibit<br>Number | Description   |
|-------------------|---|
| 31.1              | Rule 13a-14(a)/15d-14(a) Certification of Principal Executive Officer         |
| 31.2              | Rule 13a-14(a)/15d-14(a) Certification of Principal Financial Officer         |
| 32                | Certification of Periodic Financial Report Pursuant to 18 U.S.C. Section 1350 |