

POWER ONE INC
Form 10-K
March 12, 2004

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SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

ý ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES AND EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2003

Commission File No. 0-29454

POWER-ONE, INC.

(Exact name of registrant as specified in its charter)

DELAWARE

(State or other jurisdiction of incorporation or organization)

77-0420182

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

**740 Calle Plano
Camarillo, California**

(Address of principal executive offices)

93012

(Zip code)

Registrant's telephone number, including area code **(805) 987-8741**

Securities registered pursuant to Section 12(b) of the Act: **None**

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

Common Stock, \$0.001 par value

(Title of class)

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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

Aggregate market value of registrant's common stock held by non-affiliates of the registrant, based upon the closing price of a share of the registrant's common stock on June 27, 2003 as reported by the National Market System of the National Association of Securities Dealers Automated Quotation ("NASDAQ") System on that date: \$591,750,878

As of March 5, 2004, 83,657,101 shares of the registrant's \$0.001 par value common stock were outstanding.

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DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive Proxy Statement to be filed with the Securities and Exchange Commission pursuant to Regulation 14A and relating to the registrant's Annual Meeting of Stockholders For Fiscal Year 2003, to be held on May 4, 2004, are incorporated by reference into Parts II and III of this Annual Report on Form 10-K.

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Unless the context indicates otherwise, all references herein to "Power-One," "the Company," "we," "us," and "our" refer collectively to Power-One, Inc. and its subsidiaries.

This Annual Report on Form 10-K, including "Management's Discussion and Analysis of Financial Condition and Results of Operations," contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995 that can be identified by the use of forward-looking terminology such as "may," "will," "believe," "should," "expect," "anticipate," "estimate," "foresee," "plan," "intend" or "continue" or the negative thereof or other variations thereon or comparable terminology. We caution that the matters set forth under "Risk Factors," constitute cautionary statements identifying important factors with respect to such forward-looking statements, including certain risks and uncertainties that could cause actual results to differ materially from those in such forward-looking statements.

PART I

ITEM 1 BUSINESS

Overview

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We are a leading designer and manufacturer of power conversion products, most of which are sold into the communications infrastructure market. Our products are used to convert and process electrical energy to the high levels of quality, reliability and precise levels of DC voltage required by the digital economy. With hundreds of different products, we have one of the most comprehensive product lines in the power conversion industry, and are one of a few companies that can power virtually every segment of a communications infrastructure network.

Our products include:

AC/DC power supplies that power communications and networking equipment, as well as industrial, automatic/semiconductor test, transportation, medical and other electronic equipment;

DC/DC converters, including high-density and low-density products, that are generally used to control power on communications printed circuit boards;

DC power systems that are used by communications and Internet service providers;

Recently introduced DC/DC point-of-load ("POL") converters that utilize a semiconductor LGA package ideal for powering Intermediate Bus Architecture (IBA) POL applications; and

A patent-pending digital power management architecture, introduced in 2004, that integrates conversion, communications, and control for a total digital board-level solution.

We design our products primarily for the higher-end communications infrastructure market, rather than for use in personal computers, mobile phones or other consumer products.

AC/DC power supplies convert alternating current from a primary power source, such as a wall outlet, into a precisely controlled DC voltage. Virtually every electronic device that plugs into an AC wall outlet requires some type of AC/DC power supply. DC/DC converters modify an existing DC voltage level to other DC voltage levels to meet the power needs of various subsystems and components within electronic equipment. DC power systems are integrated or external systems used to power and back-up large communications infrastructure equipment.

We design our power conversion products primarily to meet the needs of manufacturers of communications infrastructure equipment. For these manufacturers, a fluctuation of power may cause severe damage to sensitive systems, resulting in data loss, file corruption and significantly reduced productivity. We design our products to take low-quality power from the electrical grid and purify it to meet the higher quality demanded by digital communications networks, providing significantly greater protection against power disturbances, such as fluctuations and outages. In addition, our products' compact designs are critical to our customers who need to minimize the space allocated to power conversion products in order to maximize the space available for other components. We continually strive to stay ahead of the technology curve to develop innovative products that meet and exceed our customers' needs.

While approximately 36.3% of our sales were to our top ten customers in 2003, we sell our products to thousands of customers worldwide. Our largest customer in 2003 was Cisco Systems, which accounted for 15.4% of our sales in 2003, 15.5% of our sales in 2002, and 15.2% of our sales in 2001. Other key communications infrastructure customers include Nokia, Nortel, Lucent, Alcatel, Hutchison 3G, Extreme Networks and Motorola. Key customers in other industries include Agilent, Siemens and Teradyne.

We were originally incorporated in 1973 as a California corporation, and re-incorporated in the State of Delaware in January 11, 1996.

Industry Background

The power conversion industry is highly fragmented and diverse. Sales of power conversion products are generally divided into two broad categories: those sold to third-party customers (merchant) and those for use in-house or sold to other divisions within the manufacturer's own company (captive). Power-One is a merchant power supply manufacturer whose products are sold to third parties.

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The communications industry experienced rapid change in the late 1990s through 2000 as deregulation and privatization fueled competition and fostered the entry of new competitors. In addition, advances in technology allowed communications service providers to offer a more varied range of services. Increases in Internet usage, demand for broadband services and demand for wireless services contributed to the growth of the communications industry. Because these technological advances required significantly greater and more reliable power, the demand for power conversion products also grew. In 2001, however, the communications infrastructure industry entered into an unprecedented downturn, which was characterized by delayed network deployments due to excess capacity by service providers and a significant inventory correction. This downturn continued into 2002, and resulted in significant downsizing and industry contraction. During this downturn we experienced decreasing sales, cancellation of orders, significant write-offs of excess inventory, restructuring charges and asset impairment charges. We experienced modest growth in 2003 compared with the low levels of 2002, as customers ordered at levels that reflected their estimated demand.

Longer term we believe the following key trends will continue to drive demand for power conversion:

Increasing Amounts of Power Required by the Communications Infrastructure Industry. With the advent of the Internet, wireless communications, broadband applications and other new technologies, recent years witnessed unprecedented growth in the volume of information being transmitted around the world at any given moment. This increase in data quantity required the construction of large-scale, sophisticated fiber optic and server-based networks in the late 1990s. However, many networks became overbuilt and excess capacity remains. Longer term, however, as the communications infrastructure industry needs to process greater amounts of data, it will in turn demand continual increases in power. Industry sources project that the amount of power required by communications infrastructure equipment will grow significantly faster than the demand by other traditional users of power.

Increasing Demand for High Reliability Power. The nature of power demanded by the digital economy is significantly different from the power provided by the electric utility grid. The electric utility grid supplies acceptable power quality, or power that is free from surges, spikes, or sags, 99.9% of the time, resulting in the equivalent of nine hours per year of interrupted, or unavailable, power. These nine hours of downtime often occur in many isolated interruptions of very short duration. In traditional industries, a brief interruption of power only interrupts operations for the time that the power is actually unavailable. For a modern communications network, however, even a minor power disturbance or brief interruption could cause computers to crash and significantly shorten the life-span of electrical components. A network crash could result in several hours of downtime, including the time necessary for complex microprocessor-based equipment to reboot and regain power. This downtime could lead to significant lost revenue and customer dissatisfaction. To reduce these risks, power conversion products convert this low-quality power to power that is much more reliable than that provided by the electric utility grid.

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Growing Use of Distributed Power Architecture and Intermediate Bus Architecture. Traditional power supply architecture uses a single, centralized power converter (supply), which distributes the power through a cable of wires to the various individual components dispersed throughout a system. Newer communications systems demand increasing amounts of power for semiconductors located throughout their communications equipment. At the same time, newer generation communications technologies being developed are requiring semiconductors that use lower voltages than previous generation technologies. In many sophisticated systems, the traditional architecture distributes power too inefficiently to accomplish these goals, because as power increases and voltage decreases, the cable thickness would have to increase to an unacceptable size.

To address this issue, Distributed Power Architecture, or DPA, uses a front-end converter (power supply) that converts AC voltage into an intermediate high-level DC voltage, typically 48 volts, thus allowing a smaller cable to be used within a system to distribute power. DC/DC converters are located throughout the system close to the devices that use power. These converters reduce the voltage to the precise amount needed at the point it is to be used. Furthermore, DPA helps to diversify the risk within a large communications system. While the failure of a traditional centralized power supply could jeopardize the entire system, the failure of a single DC/DC converter in a DPA system may only affect those few individual components that it serves. Finally, because there are many converters within the system, DPA allows for greater flexibility by permitting a part of the system to be reconfigured or upgraded without requiring a major change to the overall system.

More recently, a modified version of DPA called Intermediate Bus Architecture, or IBA, has emerged, which addresses the number of different and lower voltages required by different systems. Instead of using multiple DC/DC converters that have a typical input of 48 volts and low output voltages of less than 3V, the IBA uses a single converter with an intermediate voltage (typically between 12 volts and 3 volts). The intermediate voltage from the one converter is then transmitted to multiple POL DC/DC converters, each of which converts the intermediate voltage to the required lower voltages, which are typically 3 volts or less. During 2003 we announced a new division within the Company, Silicon Power Systems (SPS). The SPS division is engaged in the design of highly innovative and efficient silicon-based solutions for next generation DC/DC power conversion products in the IBA market. Our maXyz product line, introduced in 2003, was developed specifically for the IBA market, and in 2004, we introduced a new IBA power management solution vis-à-vis our new Z-series product line and digital controller. We spent and anticipate spending significant capital on R&D related to this developing area of power conversion technology.

Our Competitive Advantages

We believe that we have key advantages that helped us to establish a leading brand for our products. The factors that we believe contribute to this leading position are as follows:

Broad Product Line. We offer hundreds of products, in power ranging from one watt to a half-megawatt. Our smaller products are no larger than a matchbox, while our larger DC power systems could fill an entire room. With millions of potential current and voltage configurations, our broad product line offers our customers a one-stop shop opportunity, allowing them to purchase nearly all of their power conversion products from a single supplier. As a result, we are one of the few companies that can power virtually every segment of a communications infrastructure network.

Leading Design and Development Capabilities. There are a limited number of highly-skilled power engineers in the world, and we believe that we assembled some of the most capable and innovative teams in the industry. In addition to maintaining a high retention rate among our technical staff, we also added top scientists to our ranks through each of our past strategic acquisitions. This pool of engineering talent has allowed us to consistently upgrade to new generations of power conversion products, each of which has outperformed prior products with higher power density and smaller size. It

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has also allowed us to become a leader in the implementation of DPA technology, and we expect to achieve a similar leading position in IBA technology.

Reputation for Quality and Reliability. We have been in the power conversion industry since 1973. By establishing rigorous internal quality control programs, we believe that we have been able to provide our customers with products that are highly reliable. This is particularly important for manufacturers of communications infrastructure equipment. As a result, we established a strong customer base that includes many of the largest manufacturers in the communications infrastructure industry. Although power conversion products typically represent only 2% to 5% of the cost of an entire network, their failure can cripple the entire system in which they are installed. Consequently, we believe most customers are not willing to risk buying from an unproven supplier in an effort to cut costs in this area.

Changing Customer Needs. Manufacturers and service providers are facing greater competition to accelerate the time-to-market for their new products, and are increasingly expected to produce newer generations of products in a shorter period of time. As a result, they are more likely to purchase from suppliers who can offer a broad range of standardized power conversion products, rather than highly customized products that take more time to design and manufacture. Manufacturers of communications infrastructure equipment are also focusing more on their core competencies, and therefore increasingly outsourcing the manufacture of power conversion products to more efficient suppliers. Consequently, these customers are moving towards sourcing from the limited number of suppliers who can meet all of these needs.

Our Strategy: Powering the Communications Infrastructure

Our primary objective is to become one of the worldwide leaders in power conversion equipment for the global communications infrastructure equipment market. To achieve this objective, we plan to do the following:

Expand Product Lines, Including DPA and IBA Products. We provide one of the most comprehensive lines of power conversion products, including DPA and IBA products, which are increasingly being designed into communications infrastructure equipment. Once a power supply has been designed into a customer's product, it is generally difficult for the customer to change suppliers during that product's life cycle. We intend to continue our extensive research and development program to improve our products' performance and expand the breadth of our product offerings. We also intend to work with our customers to understand their changing product needs in order to proactively develop leading technology products.

Continue to Cross-Sell Products on a Global Basis. We expanded the geographic reach of our business through a series of strategic acquisitions in 1998 through 2003, which provided market penetration for our AC/DC and DC/DC products throughout Europe and broadened access for our telecom DC power systems products to Europe and Asia. We believe we have substantial opportunities to market products developed in one region to customers located in other regions. We intend to capitalize on our increased access to global markets by continuing to sell our complete product line to customers who had previously purchased only those products offered by the companies we acquired.

Continue to Acquire and Invest in Strategic Businesses and Technologies. We plan to selectively acquire and invest in businesses and technologies that can extend our geographic reach, increase the breadth of our product line, enhance the performance of our products, lower our manufacturing costs or expand our customer base in the communications infrastructure equipment market. We believe the fragmentation of the

power conversion industry presents opportunities for further consolidation. In addition, we plan to invest aggressively in internal research and development initiatives to create next-generation power conversion products; and continue to invest in advanced technologies for our DC/DC power converter products to enable significantly smaller power converters, higher efficiencies,

and better performance in controlling power on communications-oriented printed circuit boards. We have earmarked a significant portion of our overall research and development budget to develop this technology.

In 2003, we unveiled our new SPS division, which is engaged in the design of highly innovative and efficient silicon-based solutions for next generation DC/DC power conversion products in the IBA market. In 2004, we introduced a patent-pending digital power management architecture which integrates conversion, communications, and control for a total digital board-level solution. Features of this architecture and related products include the ability to fully manage up to 32 POL DC/DC converters with a single-wire digital bus. It also provides a 50% reduction in Printed Circuit Board (PCB) space, 20% cost savings, and a 90% decrease in components, number of PCB traces, and power-system development time.

Develop Technologies to Enable Alternative Energy Solutions. In recognition of and response to worldwide environmental initiatives, we increased our focus in exploring and developing new methods and approaches to the traditional DC power plant. Our efforts are directed toward core technologies and the basic building blocks that will enable the offering of reliable, cost effective, and space efficient alternative DC solutions, that can provide uninterrupted DC power without the use of any batteries. We believe that our power electronics expertise, broad product line and access to and understanding of the communications industry will help to commercialize on new energy technologies and will provide additional markets for our products.

Utilize Contract Manufacturers to Minimize Risk and Remain Cost Competitive. We continue to shift our manufacturing model toward increased use of low-cost contract manufacturers around the world, especially in Asia. Although we currently manufacture many of our products, the increased use of contract manufacturers will enable us to lower our overall costs and allow us to more efficiently scale production without significant capital investments in production capacity. We made strategic investments in or formed joint ventures with certain contract manufacturers in order to ensure adequate access to their capacity.

Our Products

The majority of our products are standard and modified standard products that are designed to accelerate customers' time to market, as well as reduce the cost of customers' new product introductions. Power supply products are generally classified as standard, modified standard and custom. Standard products refer to products that are standard to a particular manufacturer, as opposed to an industry standard. Modified standard products are a specific company's standard products modified to fit a particular customer application. Because they have already been designed and manufactured, standard and modified standard products allow end customers to reduce their time-to-market and minimize costs for new product introductions. Custom products are usually designed from "scratch" to meet the specifications of a unique customer application. Standard and modified standard products tend to have higher margins than custom products, which require significant tool and die costs and four- to six-month lead-times from conception through production. In addition, users of custom products frequently have high-volume production requirements and typically operate in more price-sensitive industries. We also developed modular product architectures, which are meant to achieve the flexibility of a custom power supply without the long lead-times and significant tool and die costs.

All of our products are designed to convert, regulate, purify, store or distribute electrical power for electronic equipment. Our products can be classified into three main groups: AC/DC power supplies, DC/DC converters and DC power systems. These categories can be distinguished based on their location, size, functions within the system and primary applications.

AC/DC power supplies:

are typically embedded within the equipment;

range in equivalent size from a small paperback book to a desktop computer;

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convert AC voltage, from a primary power source such as a wall outlet, into DC voltage(s); and

are used primarily in networking systems, large scale data processors and industrial equipment.

DC/DC converters ("bricks") and POLs:

are embedded within the equipment, and are generally mounted directly on the printed circuit boards;

bricks range in equivalent size from an AA battery to a portable CD player;

POLs may be silicon-based, and range in equivalent size from a dime to a small matchbox;

modify DC voltage into other levels of DC voltage(s) and are the cornerstone of DPA and IBA technology; and

are used primarily to power communications infrastructure equipment, although their usage is expanding to other markets.

DC power systems:

can be either stand-alone units that are external to the equipment or sub-systems that are integrated into an OEM's system;

range in size from a shelf of integrated modules to large-scale systems that can fill an entire room;

convert AC voltage into DC voltage and, together with a generator or an array of batteries, provide several hours of additional power capacity in the event of an AC input disturbance; and

are used primarily to power communications networks and cellular communications systems.

Strategic Acquisitions and Division Structure

During the industry downturn in 2001 and 2002, we restructured the Company into two primary divisions: the Compact Advanced Power Systems ("CAPS") and the Energy Solutions ("ES") divisions. The CAPS division consists of our AC/DC and DC/DC businesses, while ES represents our DC power systems business. In 2003, two additional divisions were added when we acquired di/dt Inc., a technology leader in the DC/DC space, and announced the formation of a new division within the Company, Silicon Power Systems ("SPS") division, which is focused on designing next-generation silicon-based DC/DC technology. In 2004, SPS unveiled a new all-digital power management architecture for the Intermediate Bus Architecture and its Z-series maXyz products designed specifically for that market.

Customers

We sell our power conversion products to a diversified group of thousands of equipment manufacturers, including contract manufacturers. Cisco Systems accounted for 15.4% of our sales in 2003, 15.5% of our sales in 2002, and 15.2% of our sales in 2001. Cisco Systems was the only customer to account for more than 10% of our sales during these periods.

Our top 10 customers accounted for approximately 36.3% of net sales in 2003, 39.4% of net sales in 2002, and 45.0% of net sales in 2001. Although our sales are diversified across many end markets,

our strategy has been to focus our sales efforts on the communications infrastructure equipment market. This strategy was implemented primarily due to the suitability of our products for this market and to take advantage of the higher level of long-term growth being experienced by the communications industry in the 1990s. The following table illustrates the percentage of our net sales in our primary markets:

	Year Ended December 31,	
	2003	2002
Communications	62%	64%
Industrial	16%	16%
Transportation	8%	6%
ATE/Semiconductor test equipment	5%	5%
Medical	3%	3%
Computer and Retail	3%	3%
Other	3%	3%
Total	100%	100%

We have manufacturing and research and development operations in the United States, Dominican Republic, Switzerland, Slovakia, Norway, Ireland and China. The following table summarizes our revenues and long lived assets in different geographic locations (in millions):

	Year Ended December 31,		
	2003	2002	2001
Revenues:(a)			
United States	\$ 96.0	\$ 91.0	\$ 189.1
Canada	13.8	10.1	29.7
United Kingdom	16.1	17.8	33.7
Other European countries	80.2	66.0	68.3
Malaysia	25.7	21.9	5.9
Other Asia countries	19.8	15.2	27.2
Other foreign countries	4.7	8.7	9.8
Total	\$ 256.3	\$ 230.7	\$ 363.7
Long-Lived Assets:			
United States	\$ 70.4	\$ 67.9	
Norway	12.1	8.4	
Dominican Republic	10.3	18.5	
Switzerland	19.7	19.4	
Other foreign countries	9.0	19.9	
Total	\$ 121.5	\$ 134.1	

(a)

Revenues are attributable to countries based on location of customer.

Sales and Marketing

We market our products through a global sales force. We have direct sales offices in Europe, North America, Asia and Australia. These direct sales offices are augmented by an extensive network of manufacturers' representatives and distributors. Additionally, we sell products in Asia through our joint venture in China.

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Our direct sales force is typically oriented towards customers that have the potential to purchase large volumes of our products, generally several million dollars or more on an annual basis. Our direct sales force works closely with our existing and potential customers to determine their long-term technology requirements for power conversion products. This close collaboration allows us to design products that best fit our customers' expected applications. We expect that our direct sales to strategic accounts will increase in the future as we increasingly focus on sales to these customers.

Research, Development and Engineering

Worldwide we have approximately 280 employees in our research and development departments of which approximately 170 are engineers. We spent approximately \$28.5 million on research and development in 2003, \$21.2 million in 2002, and \$23.5 million in 2001. We have four engineering and design centers in the United States: Andover, Massachusetts; and Camarillo, Carlsbad and Morgan Hill, California. We also have engineering and design centers in Santo Domingo, Dominican Republic; Drammen, Norway; Uster, Switzerland; Shenzhen, China; and Limerick, Ireland. Additionally, we have engineering staff on site in each of our manufacturing facilities. Finally, we have engineering teams at each of our power plant system integration facilities to enable more efficient customization of our system configurations for our customers. Our goal has been to establish research centers in areas that are strategically located for servicing our customers and in which we have strong access to technical talent.

Manufacturing Process and Quality Control

Production of most of our products typically entails subassembly of sophisticated printed circuit boards that are in turn combined with structural hardware to produce a final product. In response to market demands for increased quality and reliability, design complexity, and sophisticated technology, we continue to invest in state-of-the-art processes and automated many electronic assembly and testing processes that we previously performed manually. We also standardized many of our manufacturing processes and much of our equipment worldwide to increase efficiency and optimize flexibility between facilities.

Our manufacturing processes are designed to rapidly produce a wide variety of quality products at a low cost. The use of surface mount technology, or SMT, permits us to reduce board size by eliminating the need for holes in the printed circuit boards and by allowing us to use smaller components. Our investment in SMT has significantly increased our product development processes and production capacity, and we believe it has also improved our product quality. In addition, we made an equity investment in and have manufacturing outsourcing arrangements with a contract manufacturer in Asia that also employs SMT, and we have outsourcing arrangements with other contract manufacturers.

Product quality and responsiveness to our customers' needs are of critical importance in our efforts to compete successfully. We emphasize quality and reliability in both the design and manufacturing of our products. In addition to testing throughout the design and manufacturing process, we test and/or burn-in our products using automated equipment and customer-approved processes. We also perform out-of-box test or pre-ship audit on randomly selected units before delivery. We require the same levels of quality from our contract manufacturers.

As their operations expand internationally, our customers increasingly require that their power products meet or exceed established international safety and quality standards. In response to this need, we design and manufacture our power conversion products in accordance with the certification requirements of many international agencies. While not all products require the same certifications, these agencies include Underwriters Laboratories in the U.S., the CSA International in Canada, and TUV Product Service for the European market; additionally, various equipment may be tested to

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NEBS requirements for the U.S. telecom market, and to ETSI requirements for the European Union telecom market.

We manufacture and assemble approximately 50% our products at our facilities in the Dominican Republic, Norway, California, Asia, and Slovakia. We have smaller system integration facilities throughout Europe, Asia, North America, and Australia for our DC power plant products. Production of our silicon-based POLs is outsourced to contract manufacturers. Our manufacturing plant in Mexico was closed in late 2002. All of our facilities are ISO 9000 certified or, in the case of the newest facilities, are in the process of receiving their certification. In our global manufacturing operations, we currently have an aggregate of approximately 500,000 square feet of manufacturing space. Our subcontractors are primarily located in Asia.

In addition to our own facilities, we utilize low-cost contract manufacturing in several locations around the world. Although we currently manufacture many of our own products, we are shifting toward increased use of contract manufacturers to minimize costs and capital requirements, while providing greater flexibility. Though decisions to use and/or expand contract manufacturing will depend on a number of factors, including customer needs, we expect that the overall trend toward increased use of contract manufacturers will continue in the future.

Suppliers

We maintain a network of suppliers for components and other materials used in the manufacture of our power conversion products. We typically design products using components readily available from several sources and attempt to minimize our use of components that we can obtain through only one source. We procure components based upon our enterprise resource planning system and use a combination of forecasts, customer purchase orders and formal purchase agreements to create our materials requirements plan.

We occasionally use components or other materials for which a single supplier is the only source of supply. We may seek to establish long-term relationships with such suppliers. We have a number of volume purchase agreements with certain suppliers of key items. This practice enables us to maintain a more constant source for required supplies, reduce inventory expenses and produce substantial cost savings through volume purchase discounts.

Backlog

We generally sell our products pursuant to purchase orders rather than long-term contracts. Backlog consists of purchase orders on-hand having delivery dates scheduled within the next six months. Customers may cancel or reschedule most deliveries without penalty. Our backlog is not necessarily a reliable indicator of future revenue because a significant portion of customer orders is turns business (orders booked and shipped within the same reporting period that never appear as period-end backlog). In addition, customers on Vendor Managed Inventory ("VMI") programs exercise discretion as to the timing of inventory consumption. When VMI programs are initiated by customers, bookings are canceled and replaced by a product-use forecast. We then manufacture product for the customer per the forecast, and the customer uses the inventory as needed. Under a VMI program, the booking and billing occur simultaneously upon use of the product, and therefore there is always a book-to-bill ratio of 1.0 for these programs. We may bring additional VMI programs on-line in the future, which would result in higher turns business and a lower backlog.

Competition

The power conversion industry is highly fragmented and characterized by intense competition. No single company dominates the overall market, and our competitors vary depending upon the specific type of products they produce. We believe that the principal bases of competition in our targeted

markets are breadth of product line, quality, reliability, technical knowledge, flexibility, readily available products, financial strength and competitive prices. Our competition includes companies located throughout the world, including Artesyn Technologies, Vicor, Delta Electronics, Eltek, and divisions of Emerson Electric and Tyco International.

Intellectual Property Matters

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We regard certain equipment, processes, information and knowledge that we developed and use to design and manufacture our products as proprietary. We rely on a combination of patent, trade secret and other intellectual property laws, confidentiality agreements executed by most of our employees and other measures to protect our proprietary rights. We currently hold 56 patents, an increase of 11 patents from the prior year, many of which are protected by corresponding foreign patents in selected jurisdictions. Additional U.S. and foreign patent applications are pending. We hold 9 U.S. registered trademarks with additional applications pending, and claim common law trademark rights to certain additional marks.

Employees

At December 31, 2003, we employed 2,371 employees at our facilities in the following functions:

Function	Number of Employees
Manufacturing	1,609
Engineering	280
General and administrative	249
Sales and marketing	139
Quality assurance	94
Total	2,371

We believe that our continued success depends, in part, on our ability to attract and retain qualified personnel. We consider our relations with our employees to be good. None of our employees are represented by a union.

Company Website, Corporate Governance Website and Access to Company Filings

The Company posts all periodic reports on Form 10-K and 10-Q, current reports on Form 8-K, and amendments to these reports filed or furnished pursuant to the Securities Exchange Act of 1934 on its website at www.power-one.com, as soon as reasonably practicable after the reports are filed with or furnished to the Securities and Exchange Commission. Access to these reports is free of charge. In addition, the Company has launched a Corporate Governance section on its Website in response to recent legislation and the investor community's general concerns regarding corporate governance.

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RISK FACTORS

Negative communications infrastructure industry growth since 2000, coupled with general economic turmoil and uncertainty, has caused a reduction in demand for our products; if these trends continue, our operating results may continue to be materially adversely affected.

Our sales to the communications infrastructure industry increased from 25% of our total sales in 1998 to 70% for the year ended December 31, 2000. Growth in the communications industry in the late 1990s through 2000 was being driven primarily by the expansion of the Internet, broadband and wireless networks. The subsequent downturn in the industry and overall uncertainties in the world economy caused a sharp decrease in demand for our products as a result of a decrease in capital spending by our customers, particularly service providers. The industry downturn caused some of our customers, including our largest customers, to restructure into smaller operations and hampered their ability to forecast accurately. Our future revenue growth depends in large part on the resumed growth of these services as widely used media for commerce and communication. We experienced modest revenue growth in 2003 compared to 2002, and expect further revenue growth in 2004 compared with 2003. However, if the communications infrastructure industry does not continue its growth, it could have a material adverse effect on our operating results.

Cancellations, reductions or delays in purchases could cause our quarterly results to fluctuate.

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We do not obtain long-term purchase orders or commitments from our customers, and customers may generally cancel, reduce or postpone orders without penalty. Cancellations, reductions and delays in orders could reduce our backlog and adversely affect our net sales, gross profit and operating results. Our expense levels are based, in part, on expected future revenues and are relatively fixed once set. Our expectations for net sales beyond 90 days are based partially on our own estimate of future demand and partially on firm customer orders. Because a substantial portion of our quarterly net sales is made in the last month of a quarter, we are limited in our ability to reduce expenses quickly if for any reason net sales do not meet our expectations in a particular period. Therefore, fluctuations in net sales, particularly if customers cancel, postpone or delay orders, may adversely impact our operating results.

Fluctuations in customer needs may also affect our mix of products and volume of orders, which in turn affect our gross margin and operating results. High-volume orders, especially orders which require modification of our standard products, if cancelled, may substantially increase the risk of inventory obsolescence and write-offs due to excess capacity. In addition, certain significant customers are on vendor managed inventory, or VMI, programs. For VMI programs, we build product to the customers' forecast and the inventory is physically located at a site controlled by the customer. The customer pulls the inventory as needed, and the sale occurs at that time. We experienced and expect to continue to experience variability as to the timing of customers' VMI pulls, which results in variability in our net sales.

We rely on a few major customers for a material portion of our business and the loss of any of those customers could reduce our net income and operating results.

A few customers account for a material portion of our net sales each year. Cisco Systems represented 15.4% of our net sales in 2003 and 15.5% in 2002. For 2003 and 2002, our top five original equipment manufacturers ("OEM") customers accounted for approximately 28.5% and 31.6% of our net sales, respectively. If we lose any of these customers or if any of them reduces or cancels a significant order, our net sales and operating results could decrease significantly.

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Failure to anticipate trends in the type of power conversion products our customers will demand may adversely affect our business.

Because we have many customers in the communications industry, the factors and economic trends that affect these companies also affect our business. The communications industry has experienced rapid change in recent years. With advances in technology, communications service providers offer a more varied range of services. In particular, increasing Internet usage, the emerging demand for broadband services and the increasing demand for wireless services contributed to the growth of the communications industry. Because these technological advances required significantly greater and more reliable power, the demand for newer generation power conversion products has also grown. To respond to the needs of our customers in the communications industry, we must continuously develop new and more advanced products at lower prices. We made and will continue to make significant investments in next generation technologies related to our DC/DC business, but there can be no assurance that the technology will be successful.

During 2003 we announced the creation of a new division within the Company dedicated to developing next-generation DC/DC products, and this division launched its first products during 2003. Many of these new products are silicon-based, which may expose us to new and unfamiliar competitors. We also have limited experience in the semiconductor industry. In addition, some of our traditional competitors are actively seeking and forming alliances with other silicon-focused technology companies to address the same market as we are seeking to address. There can be no assurance that our products will be accepted in the marketplace. Our inability to properly assess developments in the communications industry or to anticipate the needs of our customers could cause us to lose some or all of these customers, prevent us from obtaining new customers, or cause us to record substantial write-offs for investments we are making in new technologies.

Price erosion may have a material adverse effect on our margins and profitability.

The power supply manufacturing industry is generally characterized by intense competition. We believe that the principal bases of competition in our targeted markets are breadth of product line, quality, reliability, stability and reputation of the provider, technical knowledge, flexibility and readily available products. We believe that price becomes a more important competitive factor when competition increases, when an economic downturn occurs or when we negotiate high volume orders. We saw an increase in pricing pressure from some of our key customers during 2003 and 2002 and factored additional price erosion into our forecast for 2004. Downward pricing pressure could have a material adverse effect on our operating results.

We are subject to credit risks.

The industry downturn has increased, and could continue to increase, our exposure to our customers' credit risk and the risk that our customers will not be able to fulfill their payment obligations to us.

Some of our customers experienced and may continue to experience financial difficulties and/or failed to meet their financial obligations to us. As a result, we incurred charges for bad debt provisions related to certain trade receivables. In certain cases where our end-customers utilize contract manufacturers, our accounts receivable risk may lie with the contract manufacturer and may not be guaranteed by the end-customer. If there are additional failures of our customers to meet their receivables obligations to us, or if the assumptions underlying our recorded bad debt provisions with respect to receivables obligations do not materially reflect our customers' financial conditions and payment levels, we could incur additional write-offs of receivables in excess of our provisions, which could then have a material adverse effect on our cash flow and operating results.

We face, and might in the future face, intellectual property infringement claims that might be costly to resolve.

We have from time to time received, and may in the future receive, communications from third parties asserting patent or other intellectual property rights that are alleged to cover our products. At least one such claim has resulted in pending litigation. If we do not prevail in any such litigation, our business may be adversely affected.

In addition, our industry is characterized by uncertain and conflicting intellectual property claims and vigorous protection and pursuit of intellectual property rights or positions, which have on occasion resulted in significant and often protracted and expensive litigation. We cannot assure that intellectual property claims will not be made against us in the future or that we will not be prohibited from using our technologies subject to any such claims or that we will not be required to obtain licenses and make corresponding royalty payments. In addition, the necessary management attention diverted to litigation, along with the associated legal costs, could have a significant adverse effect on operating results.

We are subject to risks associated with future company and technology acquisitions, joint ventures and strategic investments.

We intend to continue to pursue acquisitions of businesses, products and technologies, or enter into joint ventures and equity investment arrangements, that could complement or expand our business. The negotiation of potential acquisitions, joint ventures or investments as well as the integration of an acquired business, product or technology could require us to incur significant costs and cause diversion of management's time and resources. Future transactions by us could result in the following consequences:

dilutive issuances of equity securities;

incurrence of debt and contingent liabilities;

impairment of tangible and intangible assets;

research and development write-offs; and

other acquisition-related expenses.

We may also encounter difficulties in integrating acquired assets with our operations. Furthermore, we may not realize the benefits we anticipate when entering into these transactions. In addition, after we completed an acquisition, our management must be able to assume significantly greater responsibilities, and this in turn may cause them to divert their attention from our existing operations. Any of the foregoing could have a material adverse effect on our financial position and results of operations.

Any failure to protect our intellectual property could have a material adverse effect on our business; costs associated with enforcing our rights could adversely affect our results.

We rely upon a combination of patents, trademarks, contractual provisions and trade secret laws to protect our proprietary rights in certain of our products. Our competitors may, however, misappropriate our technology or independently develop technologies that are as good as, or better than, ours. Additionally, the laws of some foreign countries do not protect our proprietary rights as much as U.S. laws do. We currently own patents and continue to apply for additional patents, but the U.S. Patent and Trademark Office may reject some or all of our patent applications. The patents that the U.S. government issues to us may not provide us with a competitive advantage or create a sufficiently broad

claim to protect the technology that we develop. Furthermore, our competitors may challenge or circumvent our patents, and some of our patents may be invalidated. Litigation may be necessary to enforce our patents and other intellectual property rights, to protect our trade secrets, to determine the

validity of and scope of the proprietary rights of others or to defend against claims of infringement or invalidity. Litigation could result in substantial costs and diversion of resources and could have a significant adverse effect on operating results.

Our success depends on our ability to retain our senior management and to attract and retain key technical personnel.

If we lose one or more members of our senior management, or if we cannot attract and retain qualified management or highly technical personnel, our operating results could be adversely affected. Our capacity to develop and implement new technologies depends on our ability to employ personnel with highly technical skills. Competition for such qualified technical personnel is intense due to the relatively limited number of power supply engineers worldwide. We believe that this supply will remain constrained because of the limited number of engineering students concentrating on power conversion.

We currently have excess manufacturing capacity, and face pressure from competitors using lower cost manufacturing alternatives. Our inability to lower manufacturing costs may have a material adverse effect on our operating results.

In response to and in anticipation of our growth in the late 1990s and 2000, we made significant investments in manufacturing facilities and capital equipment. The subsequent industry downturn compelled us to close and consolidate several of our manufacturing facilities. Changes in manufacturing cost structures, including increased availability of lower-cost third party contract manufacturers, coupled with pricing pressures, and the closures and reductions of company-owned manufacturing facilities, resulted in relocation of production to alternate Company and/or third party manufacturing locations. We expect to continue to migrate our manufacturing toward third party manufacturers. We may encounter difficulties in transitioning manufacturing locations. Problems associated with such transitions may result in delays of shipments to customers, cancellations of delayed shipments, diversion of management attention, increases in inventory levels due to inability to consume inventory as planned, increases in quality issues, increases in warranty returns, and an inability to achieve anticipated manufacturing cost reductions. Any of the foregoing could have a material adverse effect on our business and results of operations.

Much of our business is subject to risks associated with operations in foreign countries.

Many of our operations are located outside of the United States and we expect to build or move additional operations overseas. Depending on location, our operations may be affected by:

imposition of tariffs, quotas, taxes and other market barriers;

restrictions on the export or import of technology;

greater difficulty in accounts receivable collection and longer collection periods;

inconsistent regulations and unexpected changes in legislation or regulatory requirements;

political and economic instability;

work stoppages and difficulties in staffing and managing international operations; and

fluctuations in the value of the U.S. dollar relative to foreign currencies.

Historically, we have not hedged against any currency exchange rate risks. The occurrence of any of these factors may adversely affect our operating results.

Our charter contains provisions that may hinder or prevent a change in control of our company.

Certain provisions of our Certificate of Incorporation could make it difficult for a third party to obtain control of us, even if such a change in control would benefit our stockholders. We have a staggered Board of Directors, which means that our stockholders can only elect approximately one third of the board at each annual meeting of stockholders. Stockholders must inform our corporate secretary before a stockholders' meeting of any business they wish to discuss and any directors they wish to nominate. Our Certificate of Incorporation also requires approval of 75% of our voting stock to amend certain provisions. Our Board of Directors can issue preferred stock without stockholder approval. Stockholder rights could be adversely affected by the rights of holders of preferred stock that we issue in the future. Finally, we have a stockholder rights plan that allows our stockholders to purchase preferred stock at a reduced price if certain parties attempt to acquire a substantial interest in us without the approval of our Board of Directors. Any one of the provisions discussed above could discourage third parties from obtaining control of us. Such provisions may also impede a transaction in which our stockholders could receive a premium over then-current market prices and our stockholders' ability to approve transactions that they consider in their best interests.

EXECUTIVE OFFICERS OF THE REGISTRANT

Set forth below is certain information concerning our executive officers.

Name	Age(1)	Position
Steven J. Goldman	46	Chief Executive Officer and Chairman of the Board
William T. Yeates	43	President and Chief Operating Officer
Eddie K. Schnopp	45	Senior Vice President Finance, Treasurer and Chief Financial Officer
Randall H. Holliday	54	Secretary and General Counsel
Donna M. Koep	43	Senior Vice President Human Resources

(1) As of March 11, 2004

Steven J. Goldman. Mr. Goldman, who joined us in 1982, became our President and Chief Executive Officer in 1990 and was named Chairman of the Board in February 1997. From 1990 to January 2000, Mr. Goldman also served as our President. He received his B.S. degree in Electrical Engineering from the University of Bridgeport and his M.B.A. degree from Pepperdine University's Executive program. Mr. Goldman is a contributing member and Co-Membership Chairman of the San Fernando Valley Chapter of the Young President's Organization.

William T. Yeates. Mr. Yeates joined us in January 2000 as President and Chief Operating Officer. Before joining us, Mr. Yeates held various positions of increasing responsibility at Lucent Technologies, including Vice President and General Manager of the Titania Power Division. He received his B.S. degree in Electrical Engineering and his M.B.A degree in Finance from Louisiana Tech University.

Eddie K. Schnopp. Mr. Schnopp, who joined us in 1981, was appointed Vice President Finance and Logistics in 1993 and Secretary and Chief Financial Officer in 1995. He was appointed Senior Vice President Finance, Treasurer and Chief Financial Officer in February 1999. From February 1999 to January 2001, Mr. Schnopp also served as our Secretary. He received his B.S. degree in Accounting from California State University Northridge. Mr. Schnopp is married to Ms. Donna Koep, our Senior Vice President Human Resources.

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Randall H. Holliday. Mr. Holliday joined us in 2000 as General Counsel, and was appointed Secretary in 2001. Before joining us, Mr. Holliday served as Secretary and General Counsel of Xircom, Inc. He has held a variety of in-house legal positions in diverse industries since 1981. Mr. Holliday received his J.D. degree in 1974 from Florida State University, Tallahassee, FL.

Donna M. Koep. Ms. Koep joined Power-One in 1978. During her employment with the Company, Ms. Koep has held numerous Human Resource management positions within the Company of increasing responsibility and scope. She was appointed in 1999 to her current position as Senior Vice President, Human Resources, responsible for overseeing and managing Power-One's worldwide Human Resource functions. Ms. Koep is married to Mr. Eddie K. Schnopp, our Senior Vice President Finance, Chief Financial Officer and Treasurer.

Our officers serve at the discretion of the Board, subject to any employment agreements.

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ITEM 2 PROPERTIES

The table below lists our principal facilities currently in operation.

Location	Approximate Size (square feet)	Employees	Primary Activity
Camarillo, California	100,000	143	Administration, R&D, Warehousing, Marketing and Sales
Carlsbad, California	65,000	72	Administration, R&D, Manufacturing, Warehousing, Marketing and Sales
Andover, Massachusetts	61,000	37	Administration, R&D, Warehousing, Marketing and Sales
Lewisville, Texas	20,000	33	Administration, R&D, Systems Integration, Warehousing, Marketing and Sales
Santo Domingo, Dominican Republic	248,000	1,342	Manufacturing and Assembly, Warehousing
Dubnica Nad Vahom, Slovakia	36,000	305	Manufacturing and Systems Integration, R&D
Uster, Switzerland	29,000	58	Administration, R&D, Small-Volume Manufacturing, Warehousing, Marketing and Sales
Limerick, Ireland	35,000	39	R&D, Small-Volume Manufacturing, Warehousing
Drammen, Norway	75,000	144	Administration, R&D, Manufacturing and Systems Integration, Warehousing, Marketing and Sales
Shenzhen, China	52,000	36	Administration, Manufacturing and Assembly, Warehousing, Marketing and Sales

The table below lists our closed facilities that are held for sale, if owned, or available for subleasing.

Location	Approximate Size (square feet)	Status
Orange County, California	157,000	Held for sublease
Round Rock, Texas	14,000	Held for sublease
San Luis, Mexico	116,000	Held for sale

We believe that the facilities we now use are more than adequate for our current and anticipated operating needs. We own our facilities in Mexico, Norway, Slovakia and Switzerland that are included in the facilities listed above. We lease the remainder of our facilities pursuant to lease agreements with expiration dates through 2014 in North America and 2009 in Europe and Asia. We believe that we will be able to renew these leases with similar terms upon expiration. If we cannot renew, we believe that we could find other suitable premises without any material

adverse impact on our operations.

ITEM 3 LEGAL PROCEEDINGS

The Company is involved in certain claims and legal proceedings, including one patent dispute that arose in the normal course of business. Management does not believe that the outcome of any of the

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claims or legal proceedings in which the Company is currently involved will have a material adverse effect on the Company's consolidated financial position, results of operations or cash flows.

VLT Corporation and Vicor Corporation v. Power-One, Inc., United States District Court, District of Massachusetts, Civil Action No. 01-10207-PBS. The Complaint, filed on February 5, 2001, alleges infringement of Vicor's U.S. patent number Re. 36,098 by certain products of Power-One. The Complaint seeks certain injunctive relief and compensatory damages. Power-One filed its Answer and Counterclaim denying all infringement and all claims by Vicor for entitlement to damages or other relief. The Company has vigorously defended the matter, denying all infringement, and aggressively refuting Vicor's projections of, and claims for, potential recoverable damages. The trial court issued its ruling on patent claims construction, and on respective summary judgment motions of Vicor and Power-One, on January 2, 2003. The court's ruling was consistent with the Company's position, and supported the Company's assertion that its accused products do not infringe the patent. The court denied both party's motions for summary judgment.

As a result of the January 2, 2003 ruling, by stipulation of Vicor and the Company (mutually agreed to for purposes of judicial efficiency and acceleration of appeal) judgment of non-infringement was entered in the Company's favor on June 20, 2003. Vicor has appealed this judgment, seeking appellate review of the January 2, 2003 claims construction ruling. For judicial economy, the appellate court has consolidated the Company's appeal with related appeals of other parties defending patent claims asserted by Vicor under the same patent at issue in the Company's case. The appellate proceedings are pending.

As part of its defense of the current patent dispute, the Company has asked for indemnification and reimbursement from escrow accounts which were created as part of the acquisitions of Melcher AG and IPD. Management believes that a substantial portion of the costs of defense, and/or ultimate award (if any) the Company may pay in this patent case will be reimbursed from amounts held in the respective escrow accounts.

ITEM 4 SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of security holders, through the solicitation of proxies or otherwise, during the fourth quarter of the fiscal year ended December 31, 2003.

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PART II

ITEM 5 MARKET FOR REGISTRANT'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS

Our Common Stock is listed on the NASDAQ and is traded under the symbol "PWER." The following table sets forth, for the quarterly periods indicated, the range of high and low closing sale prices for our common stock.

Year Ended December 31,

2003

2002

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	Year Ended December 31,			
	High	Low	High	Low
First Quarter	6.59	4.25	12.51	7.00
Second Quarter	7.93	4.56	10.18	5.53
Third Quarter	12.46	6.77	6.18	2.46
Fourth Quarter	12.03	8.16	7.90	2.40

As of March 5, 2004, there were 344 holders of record of our common stock.

We have not paid any cash dividends on our common stock and do not anticipate paying cash dividends in the foreseeable future.

Securities Authorized for Issuance Under Equity Compensation Plans

The information required by this item will be contained under the caption "Equity Compensation Plan Information as of December 31, 2003" in our definitive Proxy Statement related to our Annual Meeting of Stockholders for Fiscal Year 2003, to be held on May 4, 2004, and such information is incorporated herein by reference.

ITEM 6 SELECTED FINANCIAL DATA

In the table below, we provide selected consolidated historical financial and operating data. We prepared this information using audited financial statements for the fiscal years ended December 31, 2003, 2002, 2001, 2000 and 1999. When reading this selected historical consolidated financial and operating data, it is important to read it along with "Item 7 Management's Discussion and Analysis of

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Financial Condition and Operating Results" included in this Form 10-K. Historical results are not necessarily indicative of future results.

	Fiscal Year Ended December 31,(1)				
	2003(7)	2002(6)	2001(5)	2000(3)(4)	1999(2)(3)
(In millions, except per share amounts and percentages)					
STATEMENT OF OPERATIONS DATA:					
Net sales	\$ 256.3	\$ 230.7	\$ 363.7	\$ 511.0	\$ 237.1
Cost of goods sold	161.7	234.7	357.9	311.9	142.8
Gross profit (loss)	94.6	(4.0)	5.8	199.1	94.3
Selling, general and administrative expense					