Kimball Electronics, Inc.
Form 10-K
August 25, 2016

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-K
(Mark One)
x ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended June 30, 2016
OR
o TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission File Number 001-36454
KIMBALL ELECTRONICS, INC.
(Exact name of registrant as specified in its charter)

Indiana	35-2047713
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
1205 Kimball Boulevard, Jasper, Indiana	47546
(Address of principal executive offices)	(Zip Code)

(812) 634-4000
Registrant's telephone number, including area code
Securities registered pursuant to Section 12(b) of the Act:

Title of each Class	Name of each exchange on which registered
Common Stock, no par value	The NASDAQ Stock Market LLC

Securities registered pursuant to Section 12(g) of the Act: None
Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes o No x
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Act. Yes o No x
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 x No o
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o
Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (Section 229.405 of this chapter) 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. o
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.

Large accelerated filer o Accelerated filer x Non-accelerated filer o Smaller reporting company o
(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 o No x

The aggregate market value of the common stock held by non-affiliates, as of December 31, 2015 (the last business day of the Registrant's most recently completed second fiscal quarter), was $319.7 million based on 97.5% of common stock held by non-affiliates.

The number of shares outstanding of the Registrant's common stock as of August 15, 2016 was 28,155,140 shares.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the Annual Meeting of Share Owners to be held on October 20, 2016, are incorporated by reference into Part III.

KIMBALL ELECTRONICS, INC.
FORM 10-K INDEX

PART I
Item 1 - Business

General
As used herein, the terms “Company,” “Kimball Electronics,” “we,” “us,” or “our” refer to Kimball Electronics, Inc., the Registrant, and its subsidiaries. Reference to a year relates to a fiscal year, ended June 30 of the year indicated, rather than a calendar year unless the context indicates otherwise. Additionally, references to the first, second, third, and fourth quarters refer to those respective quarters of the fiscal year indicated.
Overview
Kimball Electronics was incorporated in 1998 and is a global provider of engineering, manufacturing, and supply chain services to customers in the automotive, medical, industrial, and public safety end markets. We offer a package of value that begins with our core competency of producing “durable electronics” and includes our set of robust processes and procedures that help us ensure that we deliver the highest levels of quality, reliability, and service throughout the entire life cycle of our customers’ products. We believe our customers appreciate our body of knowledge as it relates to the design and manufacture of their products that require durability, reliability, the highest levels of quality control, and regulatory compliance. We deliver award-winning service from our highly integrated global footprint which is enabled by a common operating system, a standardization strategy, global procedures, and teamwork. Our Customer Relationship Management (“CRM”) model is key to providing our customers convenient access to our global footprint and all of our services throughout the entire product life cycle, making us easy to do business with. Because our customers are in businesses where engineering changes must be tightly controlled and long product life cycles are common, our track record of quality, financial stability, social responsibility, and commitment to long-term relationships is important to them.
We have been producing safety critical electronic assemblies for our automotive customers for over 30 years. During this time, we have built up a body of knowledge that has not only proven to be valuable to our automotive customers, but to our medical, industrial, and public safety customers as well. We have been successful in growing and diversifying our business by leveraging our automotive experience and know-how in the areas of design and process validation, traceability, process and change control, and lean manufacturing to create valuable and innovative solutions for new customers in the medical, industrial, and public safety end market verticals. We have harmonized our quality systems to be compliant with various important industry certifications and regulatory requirements. This allows us to take advantage of other strategic points of leverage in the supply chain and within our operations so we can cost-effectively manufacture products for customers from all four of our end market verticals in the same production facility.
Many of our customers are multinational companies that sell their products in multiple regions of the world. For these customers, it is important for them to be able to leverage their investment in their supply partner relationships such that the same partner provides them with engineering, manufacturing, and supply chain services in multiple regions of the world. It is common for us to manufacture the same product for the same customer in multiple locations. Our strategy for expanding our global footprint has aligned us with the preferences of the customers in our four end market verticals and has positioned us well to support their global growth initiatives. Our global systems, procedures, processes, and teamwork combined with our CRM model have allowed us to accomplish this goal for many of our largest customers.
Our global processes and central functions that support component sourcing, procurement, quoting, and customer pricing provide commonality and consistency among the various regions in which we operate. We have a central, global purchasing organization that utilizes procurement processes and practices to help secure sources from around the world and to ensure sufficient availability of components and a uniform approach to pricing while leveraging the purchase volume of the entire organization. Customer pricing for all of the products we produce is managed centrally utilizing a standardized quoting model regardless of where our customers request their products to be produced.
Our CRM model combines members of our team from within our manufacturing facilities and members of our business development team who reside remotely and nearer to our customers around the world. We also have cross functional teams in the areas of quality, operational excellence, quoting, and design engineering with representatives

from our various locations that provide support to our teams on a global basis. The skill sets of these team members and the clarity in their roles and responsibilities help provide our customers with a strong conduit that is critical to execution and forming a strong relationship. We have institutionalized a customer scorecard process that provides all levels of our company with valuable feedback that helps us drive the actions for continuous improvement. Our customer scorecard process has helped us deliver award-winning service and build loyalty with our customers.

Our corporate headquarters is located at 1205 Kimball Boulevard, Jasper, Indiana. Production occurs in our facilities located in the United States, Mexico, Thailand, China, Poland, and Romania.

Our services are sold globally on a contract basis and we produce products to our customers' specifications. Our engineering, manufacturing, and supply chain services primarily include:

- Design services;
- Rapid prototyping and new product introduction support;
- Production and testing of printed circuit board assemblies (PCBAs);
- Industrialization and automation of manufacturing processes;
- Product design and process validation and qualification;
- Reliability testing (testing of products under a series of extreme environmental conditions);
- Assembly, production, and packaging of other related non-electronic products;
- Supply chain services; and
- Complete product life cycle management.

We pride ourselves on the fact that we pay close attention to the evolving needs and preferences of our customers. As we have done in the past, we will continue to look for opportunities to grow and diversify our business by expanding our package of value and our global footprint.

Spin-Off

Kimball Electronics, Inc. was a wholly owned subsidiary of Kimball International, Inc. ("former Parent" or "Kimball International") and on October 31, 2014 became a stand-alone public company upon the completion of a spin-off from former Parent. In conjunction with the spin-off, on October 31, 2014, Kimball International distributed 29.1 million shares of Kimball Electronics common stock to Kimball International Share Owners. Holders of Kimball International common stock received three shares of Kimball Electronics common stock for every four shares of Kimball International common stock held on October 22, 2014. Kimball International structured the distribution to be tax free to its U.S. Share Owners for U.S. federal income tax purposes.

Emerging Growth Company Status

We qualify as an "emerging growth company" as defined in the Jumpstart Our Business Startups Act (the "JOBS Act"). For as long as a company is deemed to be an "emerging growth company," it may take advantage of specified reduced reporting and other regulatory requirements that are generally unavailable to other public companies. These provisions include:

- an exemption from the auditor attestation requirement in the assessment of the "emerging growth company's" internal control over financial reporting under Section 404(b) of the Sarbanes-Oxley Act of 2002 (the "Sarbanes-Oxley Act");
- an exemption from the adoption of new or revised financial accounting standards until they would apply to private companies;
- an exemption from compliance with any new requirements adopted by the Public Company Accounting Oversight Board (the "PCAOB") requiring mandatory audit firm rotation or a supplement to the auditor's report in which the auditor would be required to provide additional information about the audit and the financial statements of the issuer;
- reduced disclosure about the "emerging growth company's" executive compensation arrangements; and
- an exemption from the requirements of holding a nonbinding advisory vote on executive compensation and the requirement to obtain Share Owner approval of any golden parachutes not previously approved.

Section 107 of the JOBS Act provides that an "emerging growth company" can take advantage of the extended transition period provided in Section 7(a)(2)(B) of the Securities Act of 1933, as amended (the "Securities Act"), for complying with new or revised accounting standards. In other words, an "emerging growth company" can delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. We have elected to take advantage of this extended transition period. Our financial statements may therefore not be comparable to those of companies that comply with such new or revised accounting standards.

We would cease to be an "emerging growth company" upon the earliest of:

- the last day of the fiscal year following the fifth anniversary of the date of the first sale of our common stock pursuant to an effective registration statement filed under the Securities Act, or June 30, 2020;

- the last day of the fiscal year in which our total annual gross revenues exceed $1 billion;
- the date on which we have, during the previous three-year period, issued more than $1 billion in non-convertible debt securities; or
- the date on which we become a "large accelerated filer," as defined in Rule 12b-2 under the Securities and Exchange Act of 1934, as amended (the "Exchange Act"), which would occur if the market value of our common stock held by non-affiliates exceeds $700 million as of the last day of our most recently completed second fiscal quarter.

Reporting Segment

Operating segments are defined as components of an enterprise for which separate financial information is available that is evaluated regularly by the chief operating decision maker, or decision making group, in deciding how to allocate resources and in assessing performance. Each of our business units qualifies as an operating segment with its results regularly reviewed by our chief operating decision maker. Our chief operating decision maker is our Chief Executive Officer. Our business units meet the aggregation criteria under the current accounting guidance for segment reporting. As of June 30, 2016, all of our business units operate in the electronic manufacturing services industry with engineering, manufacturing, and supply chain services that provide electronic assemblies primarily in automotive, medical, industrial, and public safety applications, all to the specifications and designs of our customers. The nature of the products, the production process, the type of customers, and the methods used to distribute the products, all have similar characteristics. Each of our business units service customers in multiple markets and many of our customers' programs are manufactured and serviced by multiple business units. Our global processes such as component procurement and customer pricing provide commonality and consistency among the various regions in which we operate. All of our business units have similar long-term economic characteristics. As such, our business units have been aggregated into one reportable segment. See Item 6 - Selected Financial Data for more information regarding the Company's financial results.

Our Business Strategy

We intend to achieve sustained, profitable growth in the markets we serve by supporting the global growth initiatives of our customers. Key elements of executing our strategy include:

- Expanding Our Global Footprint – continue our strategy with expansion in Europe, Asia, and the Americas, including new potential country locations and/or facility expansion as our customer demands dictate; and
- Expanding Our Package of Value – enhance our core strengths and expand upon our package of value in areas such as complex system assembly, specialized processes, precision metals, and plastics.

Our Business Offerings

We offer engineering, manufacturing, and supply chain services to customers in the automotive, medical, industrial, and public safety end market verticals. Our services support the complete product life cycle of our customers' products and our processes and capabilities cover a range of products from high volume-low mix to high mix-low volume. We collaborate with third-party design services companies to bring innovative complete design solutions to our customers. We offer Design for Excellence input to our customers as a part of our standard package of value. We use sophisticated software tools to integrate the supply chain in a way that provides our customers with the flexibility their business requires. Our robust new product introduction process and our extensive manufacturing capabilities give us the ability to execute to the quality and reliability expectations in the electronics manufacturing industry.

We value our customers and their unique needs and expectations. Our customer focus and dedication to unparalleled excellence in engineering and manufacturing has resulted in proven success in the contract manufacturing industry. Personal relationships are important to us. We strive to build long-term global partnerships. Our commitment to support our customers is backed by our history and demonstrated performance over the past 50 years.

Marketing Channels

Manufacturing, engineering, and supply chain services are marketed by our business development team. We use a CRM model to provide our customers convenient access to our global footprint and all of our services throughout the entire product life cycle.

Major Competitive Factors

Key competitive factors in the electronic manufacturing services ("EMS") market include competitive pricing, quality and reliability, engineering design services, production flexibility, on-time delivery, customer lead time, test capability, and global presence. Growth in the EMS industry is created through the proliferation of electronic components in today's advanced products and the continuing trend of original equipment manufacturers in the electronics industry subcontracting the assembly process to companies with a core competence in this area. The nature of the EMS industry is such that the start-up of new customers and new programs to replace expiring programs occurs frequently. New customer and program start-ups generally cause losses early in the life of a program, which are generally recovered as the program becomes established and matures. We continue to experience margin pressures related to an overall excess capacity position in the electronics subcontracting services market and from our customers' own capacity and capabilities to in-source production. Our continuing success depends upon our ability to replace expiring customers/programs with new customers/programs.

We do not believe that we, or the industry in general, have any special practices or special conditions affecting working capital items that are significant for understanding our EMS business other than fluctuating inventory levels which may increase in conjunction with transfers of production among facilities and start-up of new programs.

Our Competitive Strengths

Our competitive strengths derive from our experience of producing safety critical electronic assemblies for automotive customers for over 30 years and leveraging this experience to create valuable and innovative solutions for customers in different industries. Our core strengths include:

- Our core competency of producing durable electronics;
- Our body of knowledge as it relates to the design and manufacture of products that require high levels of quality control, reliability, and durability;
- Our highly integrated, global footprint;
- Our CRM model and our customer scorecard process;
- Our ability to provide our customers with valuable input regarding designs for improved manufacturability, reliability, and cost;
- Our quality systems, industry certifications and regulatory compliance;
- Our integrated supply chain solutions and competitive bid process resulting in competitive raw material pricing; and
- Complete product life cycle management.

Competitors

The EMS industry is very competitive as numerous manufacturers compete for business from existing and potential customers. Our competition includes EMS companies such as Benchmark Electronics, Inc., Jabil Circuit, Inc., and Plexus Corp. We do not have a significant share of the EMS market and were ranked the 20th largest global EMS provider for calendar year 2015 by Manufacturing Market Insider in the March 2016 edition.

Locations

As of June 30, 2016, we have eight manufacturing facilities with two located in Indiana and one located in each of Florida, China, Mexico, Poland, Romania, and Thailand. We continually assess our capacity needs and evaluate our operations to optimize our service levels for supporting our customers' needs around the globe. During fiscal year 2016, the construction of our greenfield facility in Romania was completed. In addition, we acquired certain assets and assumed certain liabilities of a contract manufacturing company located in Indiana during fiscal year 2016. See Item 1A - Risk Factors for information regarding financial and operational risks related to our international operations.

Financial information by geographic area for each of the three years in the period ended June 30, 2016 is included in Note 16 - Geographic Information of Notes to Consolidated Financial Statements and is incorporated herein by reference.

Seasonality

Sales revenue of our EMS business is generally not affected by seasonality.

Customers

While the total electronic assemblies market has broad applications, our customers are concentrated in the automotive, medical, industrial, and public safety industries.

Sales by industry as a percent of net sales for each of the three years in the period ended June 30, 2016 were as follows:

	Year Ended June 30		
	2016	2015	2014
Automotive	39%	37%	37%
Medical	30%	30%	28%
Industrial	22%	24%	26%
Public Safety	7%	7%	7%
Other	2%	2%	2%
Total	100%	100%	100%

See Note 16 - Geographic Information of Notes to Consolidated Financial Statements for financial information reported by geographic area.

Included in our sales were a significant amount to Johnson Controls, Inc. (“JCI”), Philips, and ZF TRW, which accounted for the following portions of net sales:

	Year Ended June 30		
	2016	2015	2014
Johnson Controls, Inc.	1%	4%	13%
Philips	15%	15%	12%
ZF TRW	11%	9%	10%

The nature of the contract business is such that start-up of new customers to replace expiring customers occurs frequently. Our agreements with customers are often not for a definitive term and are amended and extended, but generally continue for the relevant product’s life cycle which can be difficult to predict at the beginning of a program. Our customers generally have the right to cancel a particular product, subject to contractual provisions governing the final product runs, excess or obsolete inventory and end-of-life pricing, which reduces the additional costs that we incur when a product purchase agreement is terminated. We continue to focus on diversification of our customer base. As previously announced, volumes with JCI have declined significantly due to certain JCI programs reaching end-of-life and JCI’s decision to in-source other programs. Volumes for one of our largest contracts with JCI, which accounted for approximately $46 million in sales in fiscal year 2014, declined in fiscal year 2015 to $6 million as certain JCI programs reached end-of-life. In addition, during fiscal year 2014, due to available capacity, JCI decided to in-source other programs that were manufactured by us, which accounted for approximately $33 million in sales during fiscal year 2014 and approximately $16 million in sales during fiscal year 2015. The transition to JCI’s in-sourcing occurred in stages and began in our fourth quarter of fiscal year 2014, with the transition substantially completed during fiscal year 2015. Gross profit as a percent of net sales on the JCI product approximated the overall Kimball Electronics gross margin percentage. A significant portion of that volume already has been replaced with new business.

Backlog

The aggregate sales price of production pursuant to worldwide open orders, which may be canceled by the customer subject to contractual provisions, was $171.0 million and $194.3 million as of June 30, 2016 and 2015, respectively. Substantially all of the open orders as of June 30, 2016 are expected to be filled within the next fiscal year. Open orders may not be indicative of future sales trends.

Raw Materials

Raw materials utilized in the manufacture of contract electronic products are generally readily available from both domestic and foreign sources, although from time to time the industry experiences shortages of certain components due to supply and demand forces, combined with rapid product life cycles of certain components. In addition, unforeseen events such as natural disasters can and have disrupted portions of the supply chain. We believe that maintaining close communication with suppliers helps minimize potential disruption in our supply chain.

Raw materials are normally acquired for specific customer orders and may or may not be interchangeable among products. Inherent risks associated with rapid technological changes within this contract industry are mitigated by procuring raw materials, for the most part, based on firm orders. We may also purchase additional inventory to support new product introductions and transfers of production between manufacturing facilities.

Research and Development

Research and development activities include the development of manufacturing processes, engineering and testing procedures, major process improvements, and information technology initiatives.

Research and development costs were approximately:

	Year Ended June 30		
(Amounts in Millions)	2016	2015	2014
Research and Development Costs	$9	$9	$8

Intellectual Property

Our primary intellectual property is our proprietary manufacturing technology and processes which allow us to provide very competitive electronic manufacturing services to our customers. As such, this intellectual property is complex and normally contained within our facilities. The nature of this know-how does not lend itself well to traditional patent protection. In addition, we feel the best protection strategy involves maintaining our intellectual property as trade secrets because there is no disclosure of the information to outside parties, and there is no expiration on the length of protection. For these reasons, we do not own any patents and our only registered trademark is the “Kimball” name as registered in certain categories relating to our electronics manufacturing and design services, which were assigned to us by former Parent.

Environment and Energy Matters

Our operations are subject to various foreign, federal, state, and local laws and regulations with respect to environmental matters. We believe that we are in substantial compliance with present laws and regulations and that there are no material liabilities related to such items.

We are dedicated to excellence, leadership, and stewardship in protecting the environment and communities in which we have operations. We believe that continued compliance with foreign, federal, state, and local laws and regulations which have been enacted relating to the protection of the environment will not have a material effect on our capital expenditures, earnings, or competitive position. Management believes capital expenditures for environmental control equipment during the two fiscal years ending June 30, 2018 will not represent a material portion of total capital expenditures during those years.

Our operations require significant amounts of energy, including natural gas and electricity. Federal, foreign, and state regulations may control the allocation of fuels available to us, but to date we have experienced no interruption of production due to such regulations.

Employees

As of June 30, 2016, Kimball Electronics employed approximately 4,500 people worldwide, with approximately 850 located in the U.S. and approximately 3,650 located in foreign countries. Our U.S. operations are not subject to collective bargaining arrangements. Most of our foreign operations are subject to collective bargaining arrangements, many mandated by government regulation or customs of the particular countries. We believe that our employee relations are good.

Available Information

The Company makes available free of charge through its website, http://investors.kimballelectronics.com, its annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, proxy statements, and all amendments to those reports as soon as reasonably practicable after such material is electronically filed with, or furnished to, the Securities and Exchange Commission (“SEC”). All reports the Company files with the SEC are also available via the SEC website, http://www.sec.gov, or may be read and copied at the SEC Public Reference Room located at 100 F Street, N.E., Washington, D.C. 20549. Information on the operation of the Public Reference Room may be obtained by calling the SEC at 1-800-SEC-0330. The Company’s website and the information contained therein or incorporated therein are not intended to be incorporated into this Annual Report on Form 10-K.

Forward-Looking Statements

This document contains certain forward-looking statements. These are statements made by management, using their best business judgment based upon facts known at the time of the statements or reasonable estimates, about future results, plans, or future performance and business of the Company. Such statements involve risk and uncertainty, and their ultimate validity is affected by a number of factors, both specific and general. They should not be construed as a guarantee that such results or events will, in fact, occur or be realized as actual results may differ materially from those expressed in these forward-looking

statements. The statements may be identified by the use of words such as “believes,” “anticipates,” “expects,” “intends,” “plans
“projects,” “estimates,” “forecasts,” “seeks,” “likely,” “future,” “may,” “might,” “should,” “would,” “will,” and similar express
possible to foresee or identify all factors that could cause actual results to differ from expected or historical results. We make no commitment to update these factors or to revise any forward-looking statements for events or circumstances occurring after the statement is issued, except as required by law.

The risk factors discussed in Item 1A - Risk Factors of this report could cause our results to differ materially from those expressed in forward-looking statements. There may be other risks and uncertainties that we are unable to predict at this time or that we currently do not expect to have a material adverse effect on our business. Any such risks could cause our results to differ materially from those expressed in forward-looking statements.

At any time when we make forward-looking statements, we desire to take advantage of the “safe harbor” which is afforded such statements under the Private Securities Litigation Reform Act of 1995 where factors could cause actual results to differ materially from forward-looking statements.

Item 1A - Risk Factors

The following important risk factors, among others, could affect future results and events, causing results and events to differ materially from those expressed or implied in forward-looking statements made in this report and presented elsewhere by management from time to time. Such factors, among others, may have a material adverse effect on our business, financial condition, and results of operations and should be carefully considered. Additional risks and uncertainties that we do not currently know about, we currently believe are immaterial or we have not predicted may also affect our business, financial condition, or results of operations. Because of these and other factors, past performance should not be considered an indication of future performance.

Risks Relating to Our Business

Uncertain macroeconomic and industry conditions could adversely impact demand for our products and services and adversely affect operating results.

Market demand for our products and services, which impacts revenues and gross profit, is influenced by a variety of economic and industry factors such as:

- instability of the global financial markets;
- uncertainty of worldwide economic conditions;
- volatile energy costs;
- erosion of global consumer confidence;
- general corporate profitability of Kimball Electronics’ end markets;
- credit availability to Kimball Electronics’ end markets;
- demand fluctuations in the industries we currently serve, including automotive, medical, industrial, and public safety;
- demand for end-user products which include electronic assembly components produced by Kimball Electronics;
- excess capacity in the industries in which Kimball Electronics competes; and
- changes in customer order patterns, including changes in product quantities, delays in orders, or cancellation of orders.

We must make decisions based on order volumes in order to achieve efficiency in manufacturing capacities. These decisions include determining what level of additional business to accept, production schedules, component procurement commitments, and personnel requirements, among various other considerations. We must constantly monitor the changing economic landscape and may modify our strategic direction based upon the changing business environment. If we do not react quickly enough to the changes in market or economic conditions, it could result in lost customers, decreased market share, and increased operating costs.

Over the past several years, many countries, including certain of those in North America, Europe, and Asia in which we operate, experienced slow economic growth or recession. The economic recovery of recent years may be weak and/or short-lived and recessionary conditions may return, which could result in our customers or potential customers reducing or delaying orders as well as a number of other negative effects on our business, such as increased pricing pressures, the insolvency of suppliers, which could cause production delays, the inability of customers to obtain credit, or the insolvency of customers. In addition, the uncertainties of the market and economic conditions, both in Europe and worldwide, caused by the results of the June 23, 2016 referendum on the United Kingdom exiting the European

Union could also have an adverse effect on our business and results of operations.

We are exposed to the credit risk of our customers that have been adversely affected by the instability of market conditions.

The instability of market conditions drives an elevated risk of potential bankruptcy of customers resulting in a greater risk of uncollectible outstanding accounts receivable. Accordingly, we intensely monitor our receivables and related credit risks. The realization of these risks could have a negative impact on our profitability.

Reduction of purchases by or the loss of one or more key customers could reduce revenues and profitability.

Losses of key contract customers within specific industries or significant volume reductions from key contract customers are both risks. If a current customer of Kimball Electronics merges with or is acquired by a party that currently is aligned with a competitor, or the combination creates excess capacity, we could lose future revenues. Our continuing success is dependent upon replacing expiring contract customers/programs with new customers/programs. See "Customers" in Item 1 - Business for disclosure of the net sales as a percentage of consolidated net sales for each of our significant customers during fiscal years 2016, 2015, and 2014. Regardless of whether our agreements with our customers, including our significant customers, have a definite term, our customers typically do not have an obligation to purchase a minimum quantity of products or services as individual purchase orders or other product or project specific documentation are typically entered into from time to time. Our customers generally have the right to cancel a particular product, subject to contractual provisions governing the final product runs, excess or obsolete inventory, and end-of-life pricing. As such, our ability to continue the relationships with such customers is uncertain. Significant declines in the level of purchases by key customers or the loss of a significant number of customers could have a material adverse effect on our business. In addition, the nature of the contract electronics manufacturing industry is such that the start-up of new customers and new programs to replace expiring programs occurs frequently, and new customer and program start-ups generally cause losses early in the life of a program. We can provide no assurance that we will be able to fully replace any lost sales, which could have an adverse effect on our financial position, results of operations, or cash flows.

We operate in a highly competitive environment and may not be able to compete successfully.

Numerous manufacturers within the EMS industry compete globally for business from existing and potential customers. Some of our competitors have greater resources and more geographically diversified international operations than we do. We also face competition from the manufacturing operations of our customers, who are continually evaluating the merits of manufacturing products internally against the advantages of outsourcing to EMS providers. In the past, some of our customers have decided to in-source a portion of their electronics manufacturing from us in order to utilize their excess internal manufacturing capacity. The competition may further intensify as more companies enter the markets in which we operate, as existing competitors expand capacity and as the industry consolidates.

In relation to customer pricing pressures, if we cannot achieve the proportionate reductions in costs, profit margins may suffer. The high level of competition in the industry impacts our ability to implement price increases or, in some cases, even maintain prices, which also could lower profit margins. In addition, as end markets dictate, we are continually assessing excess capacity and developing plans to better utilize manufacturing operations, including consolidating and shifting manufacturing capacity to lower cost venues as necessary.

We are an "emerging growth company" and the reduced disclosure requirements applicable to "emerging growth companies" may make our common stock less attractive to investors.

We are an "emerging growth company," as defined in the JOBS Act. For as long as we continue to be an "emerging growth company," we intend to take advantage of certain exemptions from various reporting requirements that are applicable to other public companies. Among other things, we will not be required to (1) provide an auditor's attestation report on management's assessment of the effectiveness of our system of internal control over financial reporting pursuant to Section 404 of the Sarbanes-Oxley Act, (2) comply with any new rules that may be adopted by the PCAOB requiring mandatory audit firm rotation or a supplement to the auditor's report in which the auditor would be required to provide additional information about the audit and the financial statements of the issuer, (3) comply with any new audit rules adopted by the PCAOB after April 5, 2012 unless the SEC determines otherwise, (4) comply with any new or revised financial accounting standards applicable to public companies until such standards are also applicable to private companies under Section 102(b) of the JOBS Act, (5) provide certain disclosure regarding executive compensation required of larger public companies, or (6) hold a nonbinding advisory vote on executive compensation and obtain Share Owner approval of any golden parachute payments not previously approved. Accordingly, the information that we provide Share Owners in this annual report and in our other filings with the SEC may be different than what is available with respect to other public companies. In particular, as we have elected to take advantage of the extended transition period for complying with new or revised accounting standards applicable to public companies, our financial statements may not be comparable to companies that comply with public company effective dates for such new or revised standards. We cannot predict if investors will find our common stock less attractive because we rely on these exemptions. If some investors find our common stock less attractive as a result, there may be a less active trading market for our common stock and our stock price may be more volatile and adversely affected. In addition, as we are not required to have our auditors formally attest to and report on the effectiveness of our internal control over financial reporting, we cannot predict the outcome of testing in future periods. If, once we are no longer an "emerging growth company," our independent registered public accounting firm cannot provide an unqualified attestation report on the effectiveness of our internal control over financial reporting, investor confidence and, in turn, the market price of our common stock could decline.

We will remain an "emerging growth company" until the earliest of (1) the last day of the first fiscal year in which our total annual gross revenues exceed $1 billion, (2) the date on which we are deemed to be a "large accelerated filer," as defined in Rule 12b-2 under the Exchange Act or any successor statute, which would occur if the market value of our common stock that is held by non-affiliates exceeds $700 million as of the last business day of our most recently completed second fiscal quarter, (3) the date on which we have issued more than $1 billion in non-convertible debt during the preceding three-year period, and (4) the end of the fiscal year following the fifth anniversary of the date of the first sale of our common stock pursuant to an effective registration statement filed under the Securities Act, or June 30, 2020.

We may be unable to purchase a sufficient amount of materials, parts, and components for use in our products at competitive prices, in a timely manner, or at all.

We depend on suppliers globally to provide timely delivery of materials, parts, and components for use in our products. The financial stability of suppliers is monitored by Kimball Electronics when feasible as the loss of a significant supplier could have an adverse impact on our operations. Suppliers adjust their capacity as demand fluctuates, and component shortages and/or component allocations could occur. Certain components purchased by Kimball Electronics are primarily manufactured in select regions of the world and issues in those regions could cause manufacturing delays. Maintaining strong relationships with key suppliers of components critical to the manufacturing process is essential. Price increases of commodity components could have an adverse impact on our profitability if we cannot offset such increases with other cost reductions or by price increases to customers. Materials utilized by Kimball Electronics are generally available, but future availability is unknown and could impact our ability to meet customer order requirements. If suppliers fail to meet commitments to Kimball Electronics in terms of price, delivery, or quality, it could interrupt our operations and negatively impact our ability to meet commitments to customers.

Our operating results could be adversely affected by increases in the cost of fuel and other energy sources.

The cost of energy is a critical component of freight expense and the cost of operating manufacturing facilities. Increases in the cost of energy could reduce our profitability.

We are subject to manufacturing inefficiencies due to start-up of new programs, transfer of production, and other factors.

At times, we may experience labor or other manufacturing inefficiencies due to factors such as start-up of new programs, transfers of production among our manufacturing facilities, a sudden decline in sales, a new operating system, or turnover in personnel. Manufacturing inefficiencies could have an adverse impact on our financial position, results of operations, or cash flows.

A change in our sales mix among various products could have a negative impact on the gross profit margin.

Changes in product sales mix could negatively impact our gross margin as margins of different products vary. We strive to improve the margins of all products, but certain products have lower margins in order to price the product competitively or in connection with the start-up of a new program. An increase in the proportion of sales of products with lower margins could have an adverse impact on our financial position, results of operations, or cash flows.

We may implement future restructuring efforts and those efforts may not be successful.

We continually evaluate our manufacturing capabilities and capacities in relation to current and anticipated market conditions. We may implement restructuring plans in the future, and the successful execution of those restructuring initiatives will be dependent on various factors and may not be accomplished as quickly or effectively as anticipated.

We will face risks commonly encountered with growth through acquisitions.

Our sales growth plans may occur through both organic growth and acquisitions. Acquisitions involve many risks, including:

- difficulties in identifying suitable acquisition candidates and in negotiating and consummating acquisitions on terms attractive to us;
- difficulties in the assimilation of the operations of the acquired company;
- the diversion of resources, including diverting management's attention from our current operations;
- risks of entering new geographic or product markets in which we have limited or no direct prior experience;
- the potential loss of key customers of the acquired company;
- the potential loss of key employees of the acquired company;
- the potential incurrence of indebtedness to fund the acquisition;
- the potential issuance of common stock for some or all of the purchase price, which could dilute ownership interests of our current Share Owners;
- the acquired business not achieving anticipated revenues, earnings, cash flow, or market share;
- excess capacity;
- the assumption of undisclosed liabilities; and
- dilution of earnings.

We may not be successful in launching start-up operations.

We are committed to growing our business, and therefore from time to time, we may determine that it would be in our best interest to start up a new operation. Start-up operations involve a number of risks and uncertainties, such as funding the capital expenditures related to the start-up operation, developing a management team for the new operation, diversion of management focus away from current operations, and creation of excess capacity. Any of these risks could have a material adverse effect on our financial position, results of operations, or cash flows.

If efforts to start-up new programs are not successful, this could limit sales growth or cause sales to decline.

As we depend on industries that utilize technologically advanced electronic components which often have short life cycles, we must continue to invest in advanced equipment and product development to remain competitive in this area. The start-up of new programs requires the coordination of the design and manufacturing processes. The design and engineering required for certain new programs can take an extended period of time, and further time may be required to achieve customer acceptance. Accordingly, the launch of any particular program may be delayed, less successful than we originally anticipated, or not successful at all. Difficulties or delays in starting up new programs or lack of customer acceptance of such programs could limit sales growth or cause sales to decline.

Our international operations involve financial and operational risks.

We have operations outside the United States, primarily in China, Mexico, Poland, Romania, and Thailand. Our international operations are subject to a number of risks, which may include the following:

- economic and political instability, including the uncertainties caused by the results of the June 23, 2016 referendum on the United Kingdom exiting the European Union;
- warfare, riots, terrorism, and other forms of violence or geopolitical disruption, including the recent European refugee crisis;
- compliance with laws, such as the Foreign Corrupt Practices Act, applicable to U.S. companies doing business outside the United States;
- changes in foreign regulatory requirements and laws;
- tariffs and other trade barriers;
- potentially adverse tax consequences including the manner in which multinational companies are taxed in the U.S.; and
- foreign labor practices.

These risks could have an adverse effect on our financial position, results of operations, or cash flows. In addition, fluctuations in exchange rates could impact our operating results. Our risk management strategy includes the use of derivative financial instruments to hedge certain foreign currency exposures. Any hedging techniques we implement contain risks and may not be entirely effective. Exchange rate fluctuations could also make our products more expensive than competitors' products not subject to these fluctuations, which could adversely affect our revenues and profitability in international markets.

If customers do not perceive our engineering and manufacturing services to be innovative and of high quality, our reputation could suffer.

We believe that establishing and maintaining a good reputation is critical to our business. Promotion and enhancement of our name will depend on the effectiveness of marketing and advertising efforts and on successfully providing innovative and high quality electronic engineering and manufacturing services. If customers do not perceive our services to be innovative and of high quality, our reputation could suffer, which could have a material adverse effect on our business.

Failure to effectively manage working capital may adversely affect our cash flow from operations.

We closely monitor inventory and receivable efficiencies and continuously strive to improve these measures of working capital, but customer financial difficulties, cancellation or delay of customer orders, shifts in customer payment practices, transfers of production among our manufacturing facilities, or manufacturing delays could adversely affect our cash flow from operations.

We may not be able to achieve maximum utilization of our manufacturing capacity.

Most of our customers do not commit to long-term production schedules and we are unable to forecast the level of customer orders with certainty over a given period of time. As a result, at times it can be difficult for us to schedule production and maximize utilization of our manufacturing capacity. Fluctuations and deferrals of customer orders may have a material adverse effect on our ability to utilize our fixed capacity and thus negatively impact our operating margins.

We could incur losses due to asset impairment.

As business conditions change, we must continually evaluate and work toward the optimum asset base. It is possible that certain assets such as, but not limited to, facilities, equipment, intangible assets, or goodwill could be impaired at some point in the future depending on changing business conditions. Such impairment could have an adverse impact on our financial position and results of operations.

Fluctuations in our effective tax rate could have a significant impact on our financial position, results of operations, or cash flows.

The mix of pre-tax income or loss among the tax jurisdictions in which we operate that have varying tax rates could impact our effective tax rate. We are subject to income taxes as well as non-income based taxes in both the United States and various foreign jurisdictions. Judgment is required in determining the worldwide provision for income taxes, other tax liabilities, interest, and penalties. Future events could change management's assessment. We operate within multiple taxing jurisdictions and are subject to tax audits in these jurisdictions. These audits can involve complex issues, which may require an extended period of time to resolve. We have also made assumptions about the realization of deferred tax assets. Changes in these assumptions could result in a valuation allowance for these assets. Final determination of tax audits or tax disputes may be different from what is currently reflected by our income tax provisions and accruals.

A failure to comply with the financial covenants under the Company's $50 million credit facility could adversely impact the Company.

Our credit facility requires the Company to comply with certain financial covenants. We believe the most significant covenants under this credit facility are the ratio of consolidated indebtedness minus unencumbered U.S. cash on hand in the U.S. in excess of $15 million to adjusted consolidated EBITDA and the fixed charge coverage ratio. More detail on these financial covenants is discussed in Item 7 - Management's Discussion and Analysis of Financial Condition and Results of Operations. As of June 30, 2016, we had $9.0 million in short-term borrowings under this credit facility and had total cash and cash equivalents of $54.7 million. In the future, a default on the financial covenants under our credit facility could cause an increase in the borrowing rates or make it more difficult for us to secure future financing, which could adversely affect the financial condition of the Company.

Our business may be harmed due to failure to successfully implement information technology solutions or a lack of reasonable safeguards to maintain data security.

The operation of our business depends on effective information technology systems, which are subject to the risk of security breach or cybersecurity threat, including misappropriation of assets or other sensitive information, or data corruption which could cause operational disruption. Information systems require an ongoing commitment of significant resources to maintain and enhance existing systems and develop new systems in order to keep pace with changes in information processing technology and evolving industry standards. Implementation delays, poor execution, or a breach of information technology systems could disrupt our operations, damage our reputation, or increase costs related to the mitigation of, response to, or litigation arising from any such issue.

Failure to protect our intellectual property could undermine our competitive position.

Competing effectively depends, to a significant extent, on maintaining the proprietary nature of our intellectual property. We attempt to protect our intellectual property rights, both in the United States and in foreign countries, through a combination of trademark, copyright, and trade secret laws, as well as licensing agreements and third-party non-disclosure and assignment agreements. Because of the differences in foreign laws concerning proprietary rights, our intellectual property rights do not generally receive the same degree of protection in foreign countries as they do in the United States, and therefore in some parts of the world, we have limited protections, if any, for our intellectual property. If we are unable to adequately protect our intellectual property embodied in our solutions, designs, processes, and products, the competitive advantages of our proprietary technology could be reduced or eliminated, which would harm our business and could have a material adverse effect on our results of operations and financial position.

We may be sued by third parties for alleged infringement of their intellectual property rights and incur substantial litigation or other costs.

We may be sued by third parties who allege that our products or services infringe their intellectual property rights. Such claims, regardless of their merits, could result in substantial costs and diversion of resources in the defense or settlement of such claims. In the event of a claim upheld against us, we may be required to spend a significant amount of money and effort to develop non-infringing alternatives or obtain and maintain licenses. We may not be successful in developing such alternatives or obtaining or maintaining such licenses on reasonable terms or at all, which could have a material adverse effect on our results of operations and financial position.

Our insurance may not adequately protect us from liabilities related to product defects.

We maintain product liability and other insurance coverage that we believe to be generally in accordance with industry practices. However, our insurance coverage may not be adequate to protect us fully against substantial claims and costs that may arise from liabilities related to product defects, particularly if we have a large number of defective products or if the root cause is disputed.

Our failure to maintain Food and Drug Administration (FDA) registration of one or more of our registered manufacturing facilities could negatively impact our ability to produce products for our customers in the medical industry.

To maintain FDA registration, Kimball Electronics is subject to FDA audits of the manufacturing process. FDA audit failure could result in a partial or total suspension of production, fines, or criminal prosecution. Failure or noncompliance could have an adverse effect on our reputation in addition to an adverse impact on our financial position, results of operations, or cash flows.

We are subject to extensive environmental regulation and significant potential environmental liabilities.

The past and present operation and ownership by Kimball Electronics of manufacturing plants and real property are subject to extensive and changing federal, state, local, and foreign environmental laws and regulations, including those relating to discharges in air, water, and land, the handling and disposal of solid and hazardous waste, the use of certain hazardous materials in the production of select products, and the remediation of contamination associated with releases of hazardous substances. In addition, the increased prevalence of global climate change concerns may result in new regulations that may negatively impact us. We cannot predict what environmental legislation or regulations will be enacted in the future, how existing or future laws or regulations will be administered or interpreted or what environmental conditions may be found to exist. Compliance with more stringent laws or regulations, or stricter interpretation of existing laws, may require additional expenditures by Kimball Electronics, some of which could be material. In addition, any investigations or remedial efforts relating to environmental matters could involve material costs or otherwise result in material liabilities.

Our failure to retain the existing management team, maintain our engineering, technical, and manufacturing process expertise, or continue to attract qualified personnel could adversely affect our business.

We depend significantly on our executive officers and other key personnel. The unexpected loss of the services of any one of these executive officers or other key personnel may have an adverse effect on us.

Our success also depends on keeping pace with technological advancements and adapting services to provide manufacturing capabilities which meet customers' changing needs. In addition, we must retain our qualified engineering and technical personnel and successfully anticipate and respond to technological changes in a cost effective and timely manner. Our culture and guiding principles focus on continuous training, motivating, and development of employees, and we strive to attract, motivate, and retain qualified personnel. Failure to retain and attract qualified personnel could adversely affect our business.

Turnover in personnel could cause manufacturing inefficiencies.

The demand for manufacturing labor in certain geographic areas makes retaining experienced production employees difficult. Turnover could result in additional training and inefficiencies that could impact our operating results.

Natural disasters or other catastrophic events may impact our production schedules and, in turn, negatively impact profitability.

Natural disasters or other catastrophic events, including severe weather, terrorist attacks, power interruptions, and fires, could disrupt operations and likewise our ability to produce or deliver products. Our manufacturing operations require significant amounts of energy, including natural gas and oil, and governmental regulations may control the allocation of such fuels to Kimball Electronics. Employees are an integral part of our business and events such as a pandemic could reduce the availability of employees reporting for work. In the event we experience a temporary or permanent interruption in our ability to produce or deliver product, revenues could be reduced, and business could be materially adversely affected. In addition, catastrophic events, or the threat thereof, can adversely affect U.S. and world economies, and could result in delayed or lost sales of Kimball Electronics' products. In addition, any continuing disruption in our computer systems could adversely affect the ability to receive and process customer orders, manufacture products, and ship products on a timely basis, and could adversely affect relations with customers, potentially resulting in reduction in orders from customers or loss of customers. We maintain insurance to help protect us from costs relating to some of these matters, but such may not be sufficient or paid in a timely manner to us in the event of such an interruption.

Imposition of government regulations may significantly increase our operating costs in the United States and abroad.

Legislative and regulatory reforms by the U.S. federal and foreign governments could significantly impact the profitability of Kimball Electronics by burdening us with forced cost choices that cannot be recovered by increased pricing. For example:

- The United States healthcare reform legislation passed in 2010 and upheld by the Supreme Court in 2012 is likely to increase our total healthcare and related administrative expenses as the provisions of the law become effective over time. Governmental changes or delays to the provisions may likewise drive changes in our implementation plan causing inefficiencies and increasing our implementation costs even further. The changes resulting from this healthcare reform legislation could have a significant impact on our employment practices in the U.S., our financial position, results of operations, or cash flows.
- International Traffic in Arms Regulations (ITAR) must be followed when producing defense related products for the U.S. government. A breach of these regulations could have an adverse impact on our financial condition, results of operations, or cash flows.
- Foreign regulations are increasing in many areas such as data privacy, hazardous waste disposal, labor relations, and employment practices.

Provisions of the Dodd-Frank Act relating to "Conflict Minerals" may increase our costs and reduce our sales levels.

The Dodd-Frank Wall Street Reform and Consumer Protection Act contains provisions to improve transparency and accountability concerning the supply of certain minerals originating from the Democratic Republic of Congo ("DRC") and adjoining countries that are believed to benefit armed groups. As a result, the SEC has adopted due diligence, disclosure, and reporting requirements for companies which manufacture products that include components containing such minerals, regardless of whether the minerals are actually mined in the DRC or adjoining countries. Since certain products we manufacture for our customers contain such minerals, we are required to comply with these regulations. Such regulations could decrease the availability and increase the prices of components used in our products, particularly if we choose (or are required by our customers) to source such components from different suppliers than we use now. In addition, as our supply chain is complex and the process to comply with the SEC rules is cumbersome, the ongoing compliance process is both time-consuming and costly. We may face reduced sales if we are unable to timely verify the origins of minerals contained in the components included in our products, or supply disruptions if our due diligence process reveals that materials we source originate in the DRC or adjoining countries.

Risks Relating to the Spin-Off

If the distribution pursuant to the spin-off does not qualify as a tax-free transaction, tax could be imposed on the Share Owners and former Parent and we may be required to indemnify former Parent for its tax.

In connection with the spin-off, former Parent received (i) a ruling from the Internal Revenue Service (the “IRS”) that the Parent stock unification will not cause Parent to recognize income or gain as a result of the distribution; and (ii) an opinion of

Squire Patton Boggs (US) LLP to the effect that the distribution satisfies the requirements to qualify as a tax-free transaction for U.S. federal income tax purposes under Section 355 of the Code. However, the validity of both the IRS ruling and the tax opinion is subject to the accuracy of factual representations and assumptions provided by former Parent and us in connection with obtaining the IRS ruling and the tax opinion, including with respect to post-spin-off operations and conduct of the parties. Neither former Parent nor we are aware of any facts or circumstances that would cause these statements or representations to be incomplete or untrue or cause the facts on which the opinion is based to be materially different from the facts at the time of the spin-off. However, if these representations and assumptions are inaccurate or incomplete in any material respect, including those relating to the past and future conduct of the business, then we will not be able to rely on the IRS ruling or the tax opinion.

Furthermore, the tax opinion is not binding on the Internal Revenue Service or the courts. Accordingly, the IRS or the courts may reach conclusions with respect to the spin-off that are different from the conclusions reached in the opinion. If, notwithstanding our receipt of the tax opinion, the spin-off is determined to be taxable, then (i) former Parent would be subject to tax as if it sold the Kimball Electronics common stock in a taxable sale for its fair market value; and (ii) each Share Owner who received Kimball Electronics common stock would be treated as receiving a distribution of property in an amount equal to the fair market value of the Kimball Electronics common stock that would generally result in varied tax liabilities for each Share Owner depending on the facts and circumstances.

Even if the spin-off does qualify as a tax-free transaction for U.S. federal income tax purposes, the distribution will be taxable to former Parent (but not to former Parent Share Owners) pursuant to Section 355(e) of the Code if there are one or more acquisitions (including issuances) of the stock of either us or former Parent, representing 50% or more, measured by vote or value, of the then-outstanding stock of either us or former Parent and the acquisition or acquisitions are deemed to be part of a plan or series of related transactions that include the distribution. Any acquisition of our common stock within two years before or after the distribution (with exceptions, including public trading by less-than-5% Share Owners and certain compensatory stock issuances) generally will be presumed to be part of such a plan unless that presumption is rebutted. The resulting tax liability may have a material adverse effect on both our and former Parent’s business, financial condition, results of operations, or cash flows.

Pursuant to the Tax Matters Agreement entered into in connection with the spin-off, (i) we agreed (a) not to enter into any transaction that could cause any portion of the spin-off to be taxable to former Parent, including under Section 355(e) of the Code; and (b) to indemnify former Parent for any tax liabilities resulting from such transactions; and (ii) former Parent agreed to indemnify us for any tax liabilities resulting from such transactions entered into by former Parent. In addition, under U.S. Treasury regulations, each member of former Parent’s consolidated group at the time of the spin-off (including us and our subsidiaries) is jointly and severally liable for the resulting U.S. federal income tax liability if all or a portion of the spin-off does not qualify as a tax-free transaction, and we have agreed to indemnify former Parent for a portion of certain tax liabilities incurred in connection with the spin-off under certain circumstances. These obligations may discourage, delay, or prevent a change of control of our company.

Our historical financial information may not be a reliable indicator of our future results.

The historical financial information for the periods prior to the spin-off we have included in this Annual Report on Form 10-K has been derived from former Parent’s consolidated financial statements and does not necessarily reflect what our financial position, results of operations, and cash flows would have been as a separate, stand-alone entity during the periods presented prior to the spin-off. Former Parent did not account for us, and we were not operated, as a single stand-alone entity for the periods presented prior to the spin-off even if we represented an important business segment in former Parent’s historical consolidated financial statements. In addition, the historical information is not necessarily indicative of what our results of operations, financial position, and cash flows will be in the future. In particular, following the spin-off, changes have occurred and will occur in our cost structure, funding and operations, including changes in our tax structure, increased costs associated with reduced economies of scale, and increased costs associated with becoming a public, stand-alone company. While we were profitable as part of former Parent, we cannot provide assurance that as a stand-alone company our profits will continue at a similar level.

We may be unable to achieve some or all of the benefits that we expect to achieve from the spin-off.

As an independent, publicly traded company, we believe that our business will benefit from, among other things, the alignment of our cost structure with our business objectives and improved management incentive tools. However, now that we are separate from former Parent, we may be more susceptible to market fluctuations and other adverse events than we would have been were we still a part of former Parent. In addition, we may not be able to achieve some or all of the benefits that we expect to achieve as an independent company, including additional revenues as a result of removing certain organizational conflicts of interest as a result of the spin-off, in the time we expect, if at all.

Our customers, prospective customers and suppliers might not be satisfied that our financial stability on a stand-alone basis is sufficient to satisfy their requirements for doing or continuing to do business with them.

Some of our customers, prospective customers, and suppliers may need assurances that our financial stability on a stand-alone basis is sufficient to satisfy their requirements for doing or continuing to do business with them. If our customers, prospective customers, or suppliers are not satisfied with our financial stability, it could have a material adverse effect on our ability to bid for and obtain or retain projects, our business, financial condition, results of operations, and cash flows.

We may incur greater costs as an independent company than we did when we were a part of former Parent.

As part of former Parent, we took advantage of former Parent's size and purchasing power in procuring certain goods and services such as insurance and health care benefits, and technology such as computer software licenses. We also relied on former Parent to provide various corporate functions. After the spin-off, as a separate, independent entity, we may be unable to obtain these goods, services, and technologies at prices or on terms as favorable to us as those we obtained prior to the distribution. We may also incur costs for functions previously performed by former Parent that are higher than the amounts reflected in our historical financial statements, which could cause our profitability to decrease.

We currently share directors with former Parent, which means the overlap may give rise to conflicts.

Certain members of our Board of Directors serve as directors of former Parent, but the overlapping directors do not constitute a majority of our Board members. These directors may have actual or apparent conflicts of interest with respect to matters involving or affecting us or former Parent. For example, there could be the potential for a conflict of interest when we or former Parent look at acquisitions and other corporate opportunities that may be suitable for both companies. Also, conflicts may arise if there are issues or disputes under the commercial arrangements that will exist between former Parent and us. Our Board of Directors and the Board of Directors of former Parent will review and address any potential conflict of interests that may arise between former Parent and us. Although no specific measures to resolve such conflicts of interest have been formulated, our Board of Directors and the Board of Directors of former Parent have a fiduciary obligation to deal fairly and in good faith. Our Board of Directors exercises reasonable judgment and takes such steps as they deem necessary under all of the circumstances in resolving any specific conflict of interest which may occur and will determine what, if any, specific measures, such as retention of an independent advisor, independent counsel, or special committee, may be necessary or appropriate. Any such conflict could have a material adverse effect on our business.

We have limited operating history as an independent company upon which you can evaluate our performance and, accordingly, our prospects must be considered in light of the risks that any newly independent company encounters.

We previously operated as a business segment of former Parent. We have limited experience operating as an independent company and performing various corporate functions, including human resources, tax administration, legal (including compliance with the Sarbanes-Oxley Act of 2002 and with the periodic reporting obligations of the Exchange Act), treasury administration, investor relations, internal audit, insurance, information technology, and telecommunications services, as well as the accounting for many items such as stock-based compensation, income taxes, and intangible assets. Accordingly, our prospects must be considered in light of the risks, expenses and difficulties encountered by companies in the early stages of independent business operations, all of which could have a material adverse effect on our business.

Risks Relating to Our Common Stock

Our stock price may fluctuate significantly.

The market price of our common stock may fluctuate widely, depending on many factors, some of which may be beyond our control, including:

- actual or anticipated fluctuations in our operating results due to factors related to our business;
- wins and losses on contract competitions and new business pursuits;
- success or failure of our business strategy;
- our quarterly or annual earnings, or those of other companies in our industry;
- our ability to obtain financing as needed;

- announcements by us or our competitors of significant acquisitions or dispositions;
- changes in accounting standards, policies, guidance, interpretations or principles;
- the failure of securities analysts to cover our common stock;
- changes in earnings estimates by securities analysts or our ability to meet those estimates;
- the operating and stock price performance of other comparable companies;
- the changes in customer requirements for our products and services;
- natural or environmental disasters that investors believe may affect us;

- overall market fluctuations;
- results from any material litigation or government investigation;
- changes in laws and regulations affecting our business; and
- general economic conditions and other external factors.

Stock markets in general have experienced volatility that has often been unrelated to the operating performance of a particular company. These broad market fluctuations, coupled with changes in results of operations and general economic, political, and market conditions, could adversely affect the trading price of our common stock.

Anti-takeover provisions in our organizational documents, the Tax Matters Agreement, and Indiana law could delay or prevent a change in control.

We have adopted the Amended and Restated Articles of Incorporation and the Amended and Restated Bylaws. Certain provisions of the Amended and Restated Articles of Incorporation and the Amended and Restated Bylaws may delay or prevent a merger or acquisition that a Share Owner may consider favorable. For example, the Amended and Restated Articles of Incorporation authorizes our Board of Directors to issue one or more series of preferred stock, prevents Share Owners from acting by written consent, and requires a supermajority Share Owner approval for certain business combinations with related persons. These provisions may discourage acquisition proposals or delay or prevent a change in control, which could harm our stock price. Indiana law also imposes some restrictions on potential acquirers.

Under the Tax Matters Agreement entered into in connection with the spin-off, we have agreed not to enter into any transaction involving an acquisition (including issuance) of our common stock or any other transaction (or, to the extent we have the right to prohibit it, to permit any such transaction) that could cause the distribution pursuant to the spin-off to be taxable to former Parent. We have also agreed to indemnify former Parent for any tax resulting from any such transactions. Generally, former Parent will recognize taxable gain on the distribution if there are one or more acquisitions (including issuances) of our capital stock, directly or indirectly, representing 50% or more, measured by vote or value, of our then-outstanding capital stock, and the acquisitions or issuances are deemed to be part of a plan or series of related transactions that include the distribution. Any such shares of our common stock acquired, directly or indirectly, within two years before or after the distribution (with exceptions, including public trading by less-than-5% Share Owners and certain compensatory stock issuances) will generally be presumed to be part of such a plan unless that presumption is rebutted. As a result, our obligations may limit our ability to pursue strategic transactions or engage in new business or other transactions that may maximize our business and might discourage, delay, or prevent a change of control of our company.

We cannot assure you that we will pay dividends on our stock in the future.

We have not paid any dividends on our common stock since the spin-off. The timing, declaration, amount, and payment of future dividends to our Share Owners will fall within the discretion of our Board of Directors and will depend on many factors, including our financial condition, results of operations and capital requirements, industry practice, and other business considerations that our Board of Directors considers relevant from time to time. In addition, our ability to declare and pay any future dividends is restricted by the provisions of Indiana law and covenants in our $50 million credit facility. We do not have a plan to pay future dividends at this time. There can be no assurance that we will pay a dividend in the future or continue to pay any dividend if we do commence the payment of dividends. To the extent that expectations by market participants regarding the potential payment, or amount, of any dividend prove to be incorrect, the price of our common stock may be materially and negatively affected and investors that bought shares of our common stock based on those expectations may suffer a loss on their investment.

Item 1B - Unresolved Staff Comments

None.

Item 2 - Properties

As of June 30, 2016, we had eight manufacturing facilities with two located in Indiana and one located in each of Florida, China, Mexico, Poland, Romania, and Thailand. These facilities occupy approximately 1,122,000 square feet in aggregate, of which 1,081,000 is owned and 41,000 is leased. In addition, we own a 42,000 square-foot office building to house our headquarters located in Jasper, Indiana. See Note 16 - Geographic Information of Notes to

Consolidated Financial Statements for additional information.

Generally, our manufacturing facilities are utilized at normal capacity levels on a multiple shift basis. At times, certain facilities utilize reduced shifts. Due to sales fluctuations, not all facilities were utilized at normal capacity during fiscal year 2016. We continually assess our capacity needs and evaluate our operations to optimize our service levels by geographic

region. See Item 1A - Risk Factors for information regarding financial and operational risks related to our international operations.
Significant loss of income resulting from a facility catastrophe would be partially offset by business interruption insurance coverage.
The Company holds land leases for our facilities in China and Thailand and a facility lease for one of our Indiana facilities, with these leases expiring from fiscal year 2023 to 2056. See Note 6 - Commitments and Contingent Liabilities of Notes to Consolidated Financial Statements for additional information concerning leases. In addition, we own approximately 87 acres of land which includes land where our facilities reside.

Item 3 - Legal Proceedings

We and our subsidiaries are not parties to any pending legal proceedings, other than ordinary routine litigation incidental to the business. The outcome of current routine pending litigation, individually and in the aggregate, is not expected to have a material adverse impact on our business or financial condition.

Item 4 - Mine Safety Disclosures

Not applicable.

Executive Officers of the Registrant

Our executive officers as of August 25, 2016 are as follows:

(Age as of August 25, 2016)

Name	Age	Office and Area of Responsibility
Donald D. Charron	52	Chairman of the Board and Chief Executive Officer
Michael K. Sergesketter	56	Vice President, Chief Financial Officer
John H. Kahle	59	Vice President, General Counsel, Chief Compliance Officer, and Secretary
Christopher J. Thyen	53	Vice President, Business Development
Julia A. Dutchess	65	Vice President, Human Resources
Sandy A. Smith	53	Vice President, Information Technology
Janusz F. Kasprzyk	56	Vice President, European Operations
Steven T. Korn	52	Vice President, North American Operations
Roger Chang (Chang Shang Yu)	59	Vice President, Asian Operations

Executive officers are appointed annually by the Board of Directors. The following is a brief description of the business experience during the past five or more years of each of our executive officers.

Mr. Charron is our Chairman of the Board and Chief Executive Officer. Prior to the spin-off, he served as an Executive Vice President of former Parent, a member of the Board of Directors of former Parent, and the President of the Kimball Electronics Group that now comprises Kimball Electronics following the spin-off. Mr. Charron had led the EMS segment of former Parent since joining former Parent in 1999. Mr. Charron's extensive contract electronics industry experience prior to joining former Parent, as well as his intimate knowledge of former Parent's EMS operations, provides valuable operational, strategic, and global market insights.

Mr. Sergesketter is our Vice President, Chief Financial Officer. Prior to the spin-off, he served as Vice President, Chief Financial Officer for Kimball Electronics Group that now comprises Kimball Electronics following the spin-off. Mr. Sergesketter had served in this role with former Parent since 1996.

Mr. Kahle is our Vice President, General Counsel, Chief Compliance Officer, and Secretary. Mr. Kahle was appointed Chief Compliance Officer in April 2016 in addition to his Vice President, General Counsel, and Secretary role. Prior to the spin-off, he served as Executive Vice President, General Counsel and Secretary of former Parent and had served in this role with former Parent since 2001.

Mr. Thyen is our Vice President, Business Development and has served in this role since 2008.

Ms. Dutchess is our Vice President, Human Resources and has served in this role since 1997.

Ms. Smith is our Vice President, Information Technology and has served in this role since 2004.

Mr. Kasprzyk is our Vice President, European Operations and has served in this role since 2008.

Mr. Korn is our Vice President, North American Operations and has served in this role since 2007.

Mr. Chang is our Vice President, Asian Operations and has served in this role since 2004.

PART II

Item 5 - Market for Registrant’s Common Equity, Related Share Owner Matters and Issuer Purchases of Equity Securities

Market Prices

The Company’s common stock trades on the NASDAQ Global Select Market of The NASDAQ Stock Market LLC (“NASDAQ”) under the symbol: KE. High and low sales prices by quarter for the last two fiscal years starting November 3, 2014, the date our common stock began trading on a “regular way” basis, as quoted by the NASDAQ system, were as follows:

	2016	
	High	Low
First Quarter	$13.50	$10.74
Second Quarter	$12.22	$10.29
Third Quarter	$11.77	$9.15
Fourth Quarter	$12.22	$9.98

	2015	
	High	Low
Second Quarter (November 3 - December 31, 2014)	$13.77	$5.19
Third Quarter	$14.19	$10.07
Fourth Quarter	$17.01	$12.20

The last reported sales price of our common stock on August 15, 2016, as reported by NASDAQ, was $12.24.

Dividends

We have not paid any dividends on our common stock since the spin-off. We do not have a plan to pay future dividends at this time.

Share Owners

On August 15, 2016, the Company’s common stock was owned by approximately 1,409 Share Owners of record.

Securities Authorized for Issuance Under Equity Compensation Plans

The information required by this item concerning securities authorized for issuance under equity compensation plans is incorporated by reference to Item 12 - Security Ownership of Certain Beneficial Owners and Management and Related Share Owner Matters of Part III.

Issuer Purchases of Equity Securities

On October 21, 2015, our Board of Directors approved an 18-month stock repurchase plan, authorizing the repurchase of up to $20 million worth of our common stock. At June 30, 2016, $6.8 million remained available under the repurchase program.

During fiscal year 2016, the Company has repurchased $13.2 million of common stock under the Plan. The following table contains information about our purchases of equity securities during the three months ended June 30, 2016.

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plan	Maximum Dollar Value of Shares that May Yet Be Purchased Under the Plan
April 1, 2016 - April 30, 2016	161,243	$11.16	161,243	$10,000,007
May 1, 2016 - May 31, 2016	84,764	$10.73	84,764	$9,090,723

June 1, 2016 - June 30, 2016	188,339	$ 11.96	188,339	$ 6,838,388
Total	434,346	$ 11.42	434,346	

Performance Graph

The following performance graph is not deemed to be “soliciting material” or to be “filed” with the SEC or subject to Regulation 14A or 14C under the Exchange Act or to the liabilities of Section 18 of the Exchange Act and will not be deemed to be incorporated by reference into any filing under the Securities Act or the Exchange Act, except to the extent the Company specifically incorporates it by reference into such a filing.

The graph below compares the cumulative total return to Share Owners of the Company’s common stock from November 3, 2014, the first day of trading volume in the Company’s common stock, through June 30, 2016, the last business day of the fiscal year, to the cumulative total return of the NASDAQ Stock Market (U.S.) and a peer group index for the same period of time. The peer group index is comprised of publicly traded companies in the EMS industry and includes: Benchmark Electronics, Inc., Flextronics International Ltd., Jabil Circuit, Inc., Plexus Corp., and Sanmina Corporation. The public companies included in the peer group each have a larger revenue base than we do.

The graph assumes $100 is invested in the Company’s stock and each of the two indexes at the closing market quotations on November 3, 2014, the first day of trade volume in Kimball Electronics common stock, and that dividends, if any, are reinvested. The performances shown on the graph are not necessarily indicative of future price performance.

	11/03/2014	12/31/2014	06/30/2015	12/31/2015	06/30/2016
Kimball Electronics, Inc.	$ 100.00	$ 166.48	$ 202.08	$ 152.22	$ 172.44
NASDAQ Stock Market (U.S.)	$ 100.00	$ 102.34	$ 108.38	$ 109.47	$ 106.56
Peer Group Index	$ 100.00	$ 102.03	$ 99.48	$ 99.75	$ 101.31

Item 6 - Selected Financial Data

This information should be read in conjunction with Item 8 - Financial Statements and Supplementary Data and Item 7 - Management's Discussion and Analysis of Financial Condition and Results of Operations. The Consolidated Financial Statements for periods prior to the spin-off, which occurred on October 31, 2014, were derived from the accounting records of former Parent as if we operated on a stand-alone basis. Our historical results of operations, financial position, or cash flows presented in the Consolidated Financial Statements for periods prior to the spin-off may not be indicative of what they would have been had the Company operated as a stand-alone public company for the entirety of the periods presented.

	Year Ended June 30				
(Amounts in Thousands, Except for Per Share Data)	2016	2015	2014	2013	2012
Consolidated Statements of Income Data:					
Net Sales	$842,060	$819,350	$741,530	$703,129	$616,751
Net Income (1)	$22,287	$26,205	$24,613	$21,520	$23,903
Earnings Per Share: (2)					
Basic	$0.77	$0.90	$0.84	$0.74	$0.82
Diluted	$0.76	$0.89	$0.84	$0.74	$0.82

	As of June 30				
(Amounts in Thousands)	2016	2015	2014	2013	2012
Consolidated Balance Sheet Data:					
Total Assets	$510,565	$483,257	$408,730	$367,748	$351,912
Long-Term Debt, Less Current Maturities	$—	$—	$—	$—	$—

(1) Fiscal year 2016 net income included a foreign income tax benefit of $1.8 million ($0.06 per diluted share) as a result of a favorable tax ruling related to the fiscal year 2015 capitalization of the Company's Romania subsidiary and $0.1 million ($0.01 per diluted share) of after-tax expense related to the spin-off.

Fiscal year 2015 net income included $2.4 million ($0.08 per diluted share) of after-tax expense related to the spin-off.

Fiscal year 2014 net income included $0.3 million ($0.01 per diluted share) of after-tax restructuring expenses, $3.5 million ($0.12 per diluted share) of after-tax income resulting from settlements received related to two antitrust class action lawsuits in which the Company was a member, and $2.2 million ($0.08 per diluted share) of after-tax expense related to the spin-off.

Fiscal year 2013 net income included $0.3 million ($0.01 per diluted share) of after-tax restructuring expenses.

Fiscal year 2012 net income included $2.2 million ($0.08 per diluted share) of after-tax restructuring expenses.

(2) Basic and diluted earnings per share for the periods ended prior to the spin-off on October 31, 2014 were retrospectively restated adjusting the number of Kimball Electronics shares outstanding for the stock split effective on October 16, 2014. See Note 11 - Share Owners' Equity of Notes to Consolidated Financial Statements for more information regarding the stock split.

Item 7 - Management's Discussion and Analysis of Financial Condition and Results of Operations

Spin-Off Transaction

On October 31, 2014, Kimball Electronics, Inc. (also referred to herein as "Kimball Electronics," the "Company," "we," "us," or "our") became a stand-alone public company upon the completion of a spin-off from Kimball International, Inc. ("former Parent" or "Kimball International") into two independent publicly-traded companies. Prior to the spin-off, the Consolidated Financial Statements presented herein, and discussed below, were derived from the accounting records of former Parent as if we operated on a stand-alone basis. The Consolidated Financial Statements include allocations of general corporate expenses from former Parent including, but not limited to, spin-off costs, finance, legal, information technology, human resources, employee benefits administration, treasury, risk management, and other shared services through October 31, 2014, the spin-off date. The allocations were made on a direct usage or cost incurred basis when appropriate, with the remainder allocated using various drivers including average capital deployed, payroll, revenue less material costs, headcount, or other measures. While we believe these allocations have been made on a consistent basis and are reasonable based on the relevant cost drivers, such expenses may not be indicative of the actual expenses that would have been incurred had Kimball Electronics been operating as a stand-alone company prior to the spin-off date.

Emerging Growth Company Status

The Consolidated Financial Statements are prepared in conformity with accounting principles generally accepted in the United States of America (“U.S. GAAP”) and reflect the financial position, results of operations, and cash flows of Kimball Electronics. Kimball Electronics qualifies as an “emerging growth company” as defined in the Jumpstart Our Business Startups Act (the “JOBS Act”). For as long as a company is deemed to be an “emerging growth company,” it may take advantage of specified reduced reporting and other regulatory requirements that are generally unavailable to other public companies. The JOBS Act also provides that an “emerging growth company” can delay the adoption of certain accounting standards until those standards would otherwise apply to private companies. We have elected to take advantage of this extended transition period. Our financial statements may therefore not be comparable to those of companies that comply with such new or revised accounting standards.

Business Overview

We are a global contract electronic manufacturing services (“EMS”) company that specializes in producing durable electronics for the automotive, medical, industrial, and public safety markets. Our engineering, manufacturing, and supply chain services utilize common production and support capabilities globally. We are well recognized by our customers and the EMS industry for our excellent quality, reliability, and innovative service.

A significant business challenge that we face as an independent publicly traded company is maintaining our profit margins while we look to accelerate revenue growth. During the past few years, the EMS industry as a whole has experienced slower market growth as compared to pre-recession levels, which has added pressure to an already competitive marketplace. As a mid-sized player in the EMS market, we can expect to be challenged by the agility and flexibility of the smaller, regional players and we can expect to be challenged by the scale and price competitiveness of the larger, global players.

We enjoy a unique market position between these extremes which allows us to compete with the larger scale players for high-volume projects, but also maintain our competitive position in the generally lower volume durable electronics market space. We expect to continue to effectively operate in this market space. Price increases are uncommon in the market as production efficiencies and material pricing advantages for most projects drive costs and prices down over the life of the projects. This characteristic of the contract electronics marketplace is expected to continue, which will allow us to effectively compete in the same manner as we did prior to becoming an independent company.

Key economic indicators currently point toward continued strengthening in the overall economy. However, uncertainties still exist and may pose a threat to our future growth as they have the tendency to cause disruption in business strategy, execution, and timing in many of the markets in which we compete.

The 2016 edition of The Worldwide Electronics Manufacturing Services Market, a comprehensive study on the worldwide EMS market published by New Venture Research (“NVR”), provided worldwide forecast trends for 2015 to 2020. NVR projects worldwide electronics assembly value to grow at a compound annual growth rate (“CAGR”) of 4.0% over the next five years, with the automotive market projected to grow at a CAGR of 4.3%, the medical market projected to grow at a CAGR of 3.9%, and the industrial market projected to grow at a CAGR of 3.3%.

Our focus is on the four key vertical markets of automotive, medical, industrial, and public safety. Our overall expectation for the EMS market is that of moderate growth, but with mixed demand.

The automotive end market has benefited from relative strength in the China and U.S. markets, while demand in Europe is stable. The industrial market has been impacted by lower end market demand for climate control products; however, we are seeing increased demand for smart metering and energy efficient lighting. We saw demand in the public safety market soften compared to last year due to product mix shift as well as lower demand from government agencies. Demand in the medical market remains stable. We continue to monitor the current economic environment and its potential impact on our customers.

We invest in capital expenditures prudently for projects in support of both organic growth and potential acquisitions that would enhance our capabilities and diversification while providing an opportunity for growth and improved profitability. We have a strong focus on cost control and closely monitor market changes and our liquidity in order to proactively adjust our operating costs and discretionary capital spending as needed. Managing working capital in conjunction with fluctuating demand levels is likewise key. In addition, a long-standing component of our profit sharing incentive bonus plan is that it is linked to our financial performance which results in varying amounts of compensation expense as profits change.

We continue to maintain a strong balance sheet as of the end of fiscal year 2016, which included no long-term debt and Share Owners' equity of $324 million. Our short-term liquidity available, represented as cash and cash equivalents plus the unused amount of our credit facilities, totaled $105.4 million at June 30, 2016.

In addition to the above discussion related to the current market conditions, management currently considers the following events, trends, and uncertainties to be most important to understanding our financial condition and operating performance:

- Due to the contract and project nature of the EMS industry, fluctuation in the demand for our products and variation in the gross margin on those projects is inherent to our business. Effective management of manufacturing capacity is, and will continue to be, critical to our success.
- The nature of the EMS industry is such that the start-up of new customers and new programs to replace expiring programs occurs frequently. While our agreements with customers generally do not have a definitive term and thus could be canceled at any time, we generally realize relatively few cancellations prior to the end of the product's life cycle. We attribute this to our focus on long-term customer relationships, meeting customer expectations, required capital investment, and product qualification cycle times. As such, our ability to continue contractual relationships with our customers, including our principal customers, is not certain. New customers and program start-ups generally cause losses early in the life of a program, which are generally recovered as the program becomes established and matures. Risk factors within our business include, but are not limited to, general economic and market conditions, customer order delays, increased globalization, foreign currency exchange rate fluctuations, rapid technological changes, component availability, supplier and customer financial stability, the contract nature of this industry, the concentration of sales to large customers, and the potential for customers to choose a dual sourcing strategy or to in-source a greater portion of their electronics manufacturing. The continuing success of our business is dependent upon our ability to replace expiring customers/programs with new customers/programs. We monitor our success in this area by tracking the number of customers and the percentage of our net sales generated from them by years of service as depicted in the table below. While variation in the size of program award makes it difficult to directly correlate this data to our sales trends, we believe it does provide useful information regarding our customer loyalty and new business growth. Additional risk factors that could have an effect on our performance are located within Item 1A - Risk Factors.

	Year End		
Customer Service Years	2016	2015	2014
More than 10 Years			
% of Net Sales	56 %	49 %	44 %
# of Customers	25	22	19
5 to 10 Years			
% of Net Sales	38 %	42 %	44 %
# of Customers	29	31	24
Less than 5 Years			
% of Net Sales	6 %	9 %	12 %
# of Customers	32	25	28
Total			
% of Net Sales	100%	100%	100%
# of Customers	86	78	71

- Globalization continues to reshape not only the industries in which we operate but also our key customers and competitors.
- Employees throughout our business operations are an integral part of our ability to compete successfully, and the stability of the management team is critical to long-term Share Owner value. Our career development and succession planning processes help to maintain stability in management.

Certain preceding statements could be considered forward-looking statements under the Private Securities Litigation Reform Act of 1995 and are subject to certain risks and uncertainties including, but not limited to, our ability to fully realize the expected benefits of the completed spin-off, successful integration of acquisitions and new operations, adverse changes in the global economic conditions, loss of key customers or suppliers, or similar unforeseen events. Additional risk factors that could have an effect on our performance are located within Item 1A - Risk Factors.

Results of Operations - Fiscal Year 2016 Compared with Fiscal Year 2015

	At or For the Year Ended June 30				
(Amounts in Millions, Except for Per Share Data)	2016	as a % of Net Sales	2015	as a % of Net Sales	% Change
Net Sales	$842.1		$819.4		3 %
Gross Profit	$64.5	7.7 %	$72.4	8.8 %	(11)%
Selling and Administrative Expenses	$34.8	4.2 %	$36.1	4.4 %	(3)%
Operating Income	$29.7	3.5 %	$36.4	4.4 %	(18)%
Net Income	$22.3		$26.2		(15)%
Diluted Earnings per Share	$0.76		$0.89		
Open Orders	$171.0		$194.3		(12)%

Net Sales by Vertical Market	For the Year Ended June 30		
(Amounts in Millions)	2016	2015	% Change
Automotive	$326.7	$299.2	9 %
Medical	249.2	241.7	3 %
Industrial	186.6	200.0	(7)%
Public Safety	61.1	61.3	— %
Other	18.5	17.2	8 %
Total Net Sales	$842.1	$819.4	3 %

Net sales in fiscal year 2016 increased 3% compared to net sales in fiscal year 2015 as new product awards and overall increased demand more than offset the decline from the completion of the Johnson Controls (“JCI”) exit and unfavorable foreign exchange fluctuations. The current fiscal year increase in net sales over the prior fiscal year was driven by sales growth to customers in the automotive and medical vertical markets, with the industrial vertical market down from the prior year and the public safety vertical market remaining flat with the prior year.

Sales to customers in the automotive market improved in all markets driven by new product awards and increased demand from existing customers, which offset the expected decline from JCI. Sales to customers in the medical market increased primarily due to increased demand from existing customers, the successful launch of a next generation product for one of our largest customers, and the fourth quarter acquisition of Medivative Technologies, LLC (the “acquisition”). Sales to customers in the industrial market declined partly due to lower end market demand for climate control products.

Open orders were down 12% as of June 30, 2016 compared to June 30, 2015 as open orders in all vertical markets except the industrial vertical market declined. Open orders at a point in time may not be indicative of future sales trends due to the contract nature of our business.

Gross profit as a percent of net sales declined to 7.7% in fiscal year 2016 from 8.8% in fiscal year 2015 primarily due to product mix, foreign exchange fluctuations, costs associated with new product introductions, and contracted customer price reductions.

Selling and administrative expenses decreased both as a percent of net sales and in absolute dollars compared to fiscal year 2015. The favorable impact on selling and administrative expenses of not having charges and allocations from former Parent and lower spin-off expenses in fiscal year 2016 compared to fiscal year 2015 more than offset the increase in costs associated with being an independently publicly traded company, including increased employee salary costs, and the incremental costs related to our Romania greenfield start-up. Spin-off expenses were $0.1 million in fiscal year 2016 compared to $2.6 million in fiscal year 2015.

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Other Income (Expense) consisted of the following:

Other Income (Expense)	Year Ended June 30	
(Amounts in Thousands)	2016	2015
Interest Income	$79	$36
Interest Expense	(80)	(11)
Foreign Currency/Derivative Loss	(1,292)	(1,386)
Gain (Loss) on Supplemental Employee Retirement Plan Investment	(67)	201
Other	(386)	(424)
Other Income (Expense), net	$(1,746)	$(1,584)

The revaluation to fair value of the SERP investments recorded in Other Income (Expense) is offset by the revaluation of the SERP liability recorded in Selling and Administrative Expenses, and thus there was no effect on net income. The Foreign Currency/Derivative Loss resulted from net foreign currency exchange rate movements.

Our income before income taxes and effective tax rate was comprised of the following U.S. and foreign components:

	Year Ended June 30, 2016		Year Ended June 30, 2015	
(Amounts in Thousands)	Income Before Taxes	Effective Tax Rate	Income Before Taxes	Effective Tax Rate
United States	$1,919	17.8 %	$1,195	20.0 %
Foreign	$26,057	20.5 %	$33,576	24.8 %
Total	$27,976	20.3 %	$34,771	24.6 %

The fiscal year 2016 effective tax rate of 20.3% was favorably impacted by a high mix of earnings in foreign jurisdictions which have lower statutory rates than the U.S., a foreign income tax benefit of $1.8 million recognized as a result of a favorable tax ruling related to the fiscal year 2015 capitalization of the Company's Romania subsidiary, and adjustments for domestic tax credits. The effective tax rate for fiscal year 2015 of 24.6% was unfavorably impacted by the spin-off expenses, which were primarily nondeductible in the U.S., and favorably impacted by a high mix of earnings in foreign jurisdictions which have lower statutory tax rates than the U.S.

Our overall effective tax rate will fluctuate depending on the geographic distribution of our worldwide earnings. See Note 10 - Income Taxes of Notes to Consolidated Financial Statements for more information.

We recorded net income of $22.3 million in fiscal year 2016, or $0.76 per diluted share, a decrease of 15% from fiscal year 2015 net income of $26.2 million, or $0.89 per diluted share, due to the reasons previously discussed.

A significant amount of sales to Philips and ZF TRW accounted for the following portions of our net sales:

	Year Ended June 30	
	2016	2015
Philips	15%	15%
ZF TRW	11%	9%

The nature of the EMS industry is such that the start-up of new customers and new programs to replace expiring programs occurs frequently. New customers and program start-ups generally cause losses early in the life of a program, which are generally recovered as the program becomes established and matures. Volumes declined approximately $22 million in fiscal year 2016 related to the completion of the JCI exit. A significant portion of that volume already has been replaced with new business.

Comparing the balance sheet as of June 30, 2016 to June 30, 2015, accounts receivable increased $9.8 million primarily as a result of increased sales volumes and the addition of the accounts receivable balance of the acquisition. Our inventory balance increased $7.7 million primarily to support increased production volumes and the additional inventory from the acquisition. Property and equipment, net of accumulated depreciation, increased $13.9 million primarily due to expenditures for manufacturing equipment, including equipment to support new business awards, our greenfield start-up facility in Romania, and property and equipment from the acquisition. Goodwill increased $3.6 million as a result of the acquisition. Our accounts payable balance increased $8.7 million primarily on the increased inventory purchases to support increased production volumes, the increase resulting from operations beginning at our greenfield facility in Romania, and the addition of the accounts payable balance of the acquisition. Borrowings under credit facilities increased $9.0 million for domestic cash needs including the acquisition and stock repurchases. Treasury stock, at cost increased $13.5 million primarily due to the stock repurchases under the stock repurchase program authorized by the Company's Board of Directors in October 2015.

Results of Operations - Fiscal Year 2015 Compared with Fiscal Year 2014

	At or For the Year Ended June 30				
(Amounts in Millions, Except for Per Share Data)	2015	as a % of Net Sales	2014	as a % of Net Sales	% Change
Net Sales	$819.4		$741.5		10 %
Gross Profit	$72.4	8.8 %	$61.0	8.2 %	19 %
Selling and Administrative Expenses	$36.1	4.4 %	$36.4	4.9 %	(1)%
Other General Income	$—		$5.7		
Operating Income	$36.4	4.4 %	$29.9	4.0 %	21 %
Net Income	$26.2		$24.6		6 %
Diluted Earnings per Share	$0.89		$0.84		
Open Orders	$194.3		$178.0		9 %

Net Sales by Vertical Market	For the Year Ended June 30		
(Amounts in Millions)	2015	2014	% Change
Automotive	$299.2	$275.5	9 %
Medical	241.7	210.1	15 %
Industrial	200.0	189.7	5 %
Public Safety	61.3	52.8	16 %
Other	17.2	13.4	29 %
Total Net Sales	$819.4	$741.5	10 %

Net sales in fiscal year 2015 increased 10% compared to net sales in fiscal year 2014. The fiscal year 2015 increase in net sales over fiscal year 2014 was driven by sales growth to customers in all four of our vertical markets, with the medical and public safety vertical markets experiencing double-digit growth. Despite the decline in sales to Johnson Controls, Inc. ("JCI") as discussed in further detail below, sales to customers in the automotive market improved primarily on the strength of the China market. Sales to customers in the medical market, the industrial market, and the public safety market improved from both increased demand for existing products and new product awards.

Open orders were up 9% as of June 30, 2015 compared to June 30, 2014 as the expected decline in open orders to JCI was more than offset by increased open orders to other customers. Open orders at a point in time may not be indicative of future sales trends due to the contract nature of our business.

Gross profit as a percent of net sales improved to 8.8% in fiscal year 2015 from 8.2% in fiscal year 2014 primarily due to the positive impact from leverage gained on higher revenue and lower incentive compensation costs.

Selling and administrative expenses as a percent of net sales decreased 50 basis points and decreased less than 1% in absolute dollars compared to fiscal year 2014. Current fiscal year selling and administrative expenses included spin-off expenses of $2.6 million which were $0.4 million higher than the prior fiscal year spin-off expenses of $2.2 million in addition to higher salary and employee benefit expense. The year-over-year increase in salary and employee benefit expense as a result of the spin-off was more than offset by the decline in charges and allocations not related to the spin-off from former Parent, which included incentive compensation costs.

We recorded no Other General Income during fiscal year 2015. Other General Income in fiscal year 2014 included pre-tax income of $5.7 million resulting from settlements received related to two antitrust class action lawsuits in which Kimball Electronics was a class member. The lawsuits alleged that certain EMS segment suppliers conspired over a number of years to raise and fix the prices of electronic components, resulting in overcharges to purchasers of those components.

Other income (expense) consisted of the following:

Other Income (Expense)	Year Ended June 30	
(Amounts in Thousands)	2015	2014
Interest Income	$36	$41
Interest Expense	(11)	(2)
Foreign Currency/Derivative Loss	(1,386)	(127)
Gain on Supplemental Employee Retirement Plan Investment	201	695
Other	(424)	(295)
Other Income (Expense), net	$(1,584)	$312

The revaluation to fair value of the SERP investments recorded in Other Income (Expense) is offset by the revaluation of the SERP liability recorded in Selling and Administrative Expenses, and thus there was no effect on net income. The Foreign Currency/Derivative Loss resulted from net foreign currency exchange rate movements.

Our income before income taxes and effective tax rate was comprised of the following U.S. and foreign components:

	Year Ended June 30, 2015		Year Ended June 30, 2014	
(Amounts in Thousands)	Income Before Taxes	Effective Tax Rate	Income Before Taxes	Effective Tax Rate
United States	$1,195	20.0 %	$5,412	47.6 %
Foreign	$33,576	24.8 %	$24,830	12.3 %
Total	$34,771	24.6 %	$30,242	18.6 %

The fiscal year 2015 effective tax rate of 24.6% was unfavorably impacted by the spin-off expenses, which were largely nondeductible in the U.S., and favorably impacted by a high mix of earnings in foreign jurisdictions which have lower statutory rates than the U.S and adjustments for domestic tax credits. The effective tax rate for fiscal year 2014 of 18.6% was favorably impacted by a high mix of earnings in foreign jurisdictions which have lower statutory tax rates than the U.S. The fiscal year 2014 U.S. effective tax rate was higher than the U.S. statutory rate as the majority of our expenses related to the spin-off were non-deductible. The fiscal year 2014 foreign effective tax rate benefited from $1.4 million of adjustments related to decreases in foreign deferred tax asset valuation allowances.

We recorded net income of $26.2 million in fiscal year 2015, or $0.89 per diluted share, an increase of 6% from fiscal year 2014 net income of $24.6 million, or $0.84 per diluted share, due to the reasons previously discussed.

A significant amount of sales to Philips and JCI accounted for the following portions of our net sales:

	Year Ended June 30	
	2015	2014
Philips	15%	12%
Johnson Controls, Inc.	4%	13%

The nature of the EMS industry is such that the start-up of new customers and new programs to replace expiring programs occurs frequently. New customers and program start-ups generally cause losses early in the life of a program, which are generally recovered as the program becomes established and matures. Volumes for one of our largest contracts with JCI, which accounted for approximately $46 million in fiscal year 2014, declined in fiscal year 2015 to approximately $6 million as certain JCI programs reached end-of-life. In addition, during the second quarter of our prior fiscal year, due to available capacity, JCI decided to in-source other programs that are manufactured by us, which accounted for approximately $33 million in net sales in fiscal year 2014 and approximately $16 million in net sales in fiscal year 2015. The transition to JCI's in-sourcing occurred in stages and began in our fourth quarter of fiscal year 2014 and is substantially complete. Gross profit as a percent of net sales on the JCI product approximates the overall Kimball Electronics gross margin percentage. A significant portion of that volume already has been replaced with new business.

Liquidity and Capital Resources

Working capital at June 30, 2016 was $187.4 million compared to working capital of $194.2 million at June 30, 2015. The current ratio was 2.1 at June 30, 2016 and 2.2 at June 30, 2015. Our short-term liquidity available, represented as cash and cash equivalents plus the unused amount of our credit facilities, totaled $105.4 million at June 30, 2016 and $125.1 million at June 30, 2015.

Cash Conversion Days (“CCD”) are calculated as the sum of Days Sales Outstanding (“DSO”) plus Production Days Supply on Hand (“PDSOH”) less Accounts Payable Days (“APD”). CCD for the quarter ended June 30, 2016 was 59 days, which improved from 63 days for the quarter ended June 30, 2015. The following table summarizes our CCD for the quarterly periods indicated.

	Three Months Ended				
	June 30, 2016	March 31, 2016	December 31, 2015	September 30, 2015	June 30, 2015
DSO	61	60	59	59	62
PDSOH	61	60	62	65	63
APD	63	63	62	63	62
CCD	59	57	59	61	63

We define DSO as the average of monthly trade accounts and notes receivable divided by an average day’s net sales, PDSOH as the average of monthly gross inventory divided by an average day’s cost of sales, and APD as the average of monthly accounts payable divided by an average day’s cost of sales.

Cash Flows

The following table reflects the major categories of cash flows for the fiscal years ended June 30, 2016, June 30, 2015, and June 30, 2014.

	Year Ended June 30		
(Amounts in Millions)	2016	2015	2014
Net cash provided by operating activities	$36.8	$28.1	$39.3
Net cash used for investing activities	$(42.6)	$(36.5)	$(20.0)
Net cash (used for) provided by financing activities	$(4.3)	$50.2	$(11.6)

Cash Flows from Operating Activities

Net cash provided by operating activities for the fiscal years ended June 30, 2016, June 30, 2015, and June 30, 2014 was primarily driven by net income adjusted for non-cash items. Changes in working capital used $10.0 million, $22.5 million, and $6.4 million of cash for the fiscal years ended June 30, 2016, June 30, 2015, and June 30, 2014, respectively.

The $10.0 million usage of cash from changes in working capital balances in fiscal year 2016 was primarily due to fluctuations in our accounts receivable, inventory, and prepaid expenses and other current assets. An increase in accounts receivable used cash of $9.2 million which resulted primarily from increased sales volumes. An increase in inventory used cash of $3.5 million primarily to support increased production volumes. An increase in certain prepaid expenses and other current assets used cash of $3.7 million primarily due to an increase in taxes refundable. Partially offsetting these usages was an increase in accounts payable which provided cash of $8.3 million primarily related to the increased inventory purchases.

The $22.5 million usage of cash from changes in working capital balances in fiscal year 2015 was primarily due to fluctuations in our accounts receivable and inventory. An increase in accounts receivable used cash of $14.7 million which resulted primarily from increased sales volumes and the mix of sales among customers. An increase in inventory used cash of $12.2 million primarily to support increased production volumes. Partially offsetting these usages was an increase in accounts payable which provided cash of $13.6 million primarily related to the increased inventory purchases.

The $6.4 million usage of cash from changes in working capital balances in fiscal year 2014 was due to fluctuations in our accounts receivable, inventory, accounts payable, and accrued expenses. A $10.1 million increase in accounts receivable during fiscal year 2014 resulted from the increased sales volumes in addition to a shift in the payment practices of several of our customers, and inventory increased $12.8 million during fiscal year 2014 to support increased production volumes. Partially

offsetting these increases were an increase of $9.5 million to accounts payable related to the increased inventory purchases and an increase of $8.1 million to accrued expenses primarily due to higher accrued profit-based incentive compensation.

Cash Flows from Investing Activities

For each period shown in the previous table, net cash used for investing activities primarily represents cash used for capital investments. During fiscal years 2016, 2015, and 2014, we reinvested $34.6 million, $36.9 million, and $20.8 million, respectively, into capital investments for the future with the largest expenditures in each period being for manufacturing equipment. During fiscal year 2016, a large amount of our expenditures included equipment to support new business awards, and our greenfield start-up facility in Romania. Also during fiscal year 2016, we invested $8.3 million to acquire certain assets and assumed certain liabilities (the “acquisition”) of Medivative Technologies, LLC. See Note 3 - Acquisition of Notes to Consolidated Financial Statements for more information on the acquisition.

Cash Flows from Financing Activities

Net cash used for financing activities for the fiscal year ended June 30, 2016 resulted primarily from repurchases of our common stock under an authorized stock repurchase plan, which was partially offset by net borrowings on our credit facilities. During fiscal years 2015 and 2014, net cash provided by or used for financing activities primarily represents net transfers from and to former Parent. As former Parent provided centralized treasury functions for us, cash was regularly transferred both to and from former Parent’s subsidiaries, as necessary. In connection with the spin-off, net distributions of cash were made from former Parent to us of $44.3 million on or around October 31, 2014.

Credit Facilities

In connection with the spin-off, the Company entered into a new U.S. primary credit facility (the “primary facility”) dated as of October 31, 2014 with JPMorgan Chase Bank National Association, as administrative agent, and other lenders party thereto. The credit facility has a maturity date of October 31, 2019 and allows for up to $50 million in borrowings, with an option to increase the amount available for borrowing to $75 million at the Company’s request, subject to participating banks’ consent.

The proceeds of the revolving credit loans are to be used for general corporate purposes of the Company including potential acquisitions and stock repurchases. A portion of the credit facility, not to exceed $15 million of the principal amount, will be available for the issuance of letters of credit. A commitment fee on the unused portion of the principal amount of the credit facility is payable at a rate that ranges from 20.0 to 25.0 basis points per annum as determined by the Company’s ratio of consolidated total indebtedness to adjusted consolidated EBITDA. The interest rate on borrowings is dependent on the type of borrowings.

At June 30, 2016, we had $9.0 million in short-term borrowings under the primary facility used for domestic cash needs, including the acquisition and stock repurchases, and $0.4 million in letters of credit against the primary credit facility. We had no short-term borrowings under the primary facility at June 30, 2015.

The Company’s financial covenants under the primary credit facility require:

- a ratio of consolidated total indebtedness minus unencumbered U.S. cash on hand in the U.S. in excess of $15 million to adjusted consolidated EBITDA, determined as of the end of each of its fiscal quarters for the then most recently ended four fiscal quarters, to not be greater than 3.0 to 1.0, and
- a fixed charge coverage ratio, determined as of the end of each of its fiscal quarters for the then most recently ended four fiscal quarters, to not be less than 1.10 to 1.00.

We were in compliance with the financial covenants during the fiscal year ended June 30, 2016.

Kimball Electronics utilizes foreign credit facilities to satisfy short-term cash needs at specific foreign locations rather than funding from intercompany sources. As of June 30, 2016, we maintained a Thailand overdraft credit facility which allows for borrowings up to 90 million Thai Baht (approximately $2.6 million at June 30, 2016 exchange rates). We had no borrowings outstanding under this foreign credit facility as of June 30, 2016 or June 30, 2015. As of June 30, 2016, we also maintained a credit facility for our China operation, which allows for borrowings up to $7.5 million that can be drawn in either U.S. dollars or China Renminbi. We had no borrowings outstanding under this foreign credit facility as of June 30, 2016 or June 30, 2015. During fiscal year 2016, we borrowed $3.0 million on the China credit facility for general working capital purposes and repaid the amount during the fiscal year. These foreign credit facilities can be canceled at any time by either the bank or us.

Future Liquidity

We believe our principal sources of liquidity from available funds on hand, cash generated from operations, and the availability of borrowing under our credit facilities will be sufficient to meet our working capital and other operating needs for at least the next 12 months. The availability to borrow under all of our credit facilities in USD equivalent totaled $50.7 million at June 30, 2016. We expect to continue to invest in capital expenditures prudently, particularly for projects, including potential acquisitions, that would enhance our capabilities and diversification while providing an opportunity for growth and improved profitability. As part of this plan to enhance our capabilities and diversification, subsequent to June 30, 2016, we acquired certain assets and assumed certain liabilities of Aircom Manufacturing, Inc., the former parent of Medivative Technologies, for total consideration of approximately $3.5 million.

We are growing our business in Europe through the expansion of our manufacturing capabilities in the region. We completed the construction of our greenfield facility in Romania this fiscal year and have begun operations. Capacity at this facility will continue to ramp up through fiscal year 2017.

At June 30, 2016, our capital expenditure commitments were approximately $13 million, consisting primarily of commitments for manufacturing equipment in anticipation of future growth, including new program wins. We anticipate our funds on hand and funds provided by operations will be sufficient to fund these capital expenditures.

At June 30, 2016, our foreign operations held cash totaling $33.2 million. Except for the nontaxable repayment of intercompany loans, our intent is to permanently reinvest these funds outside of the United States and our current plans do not demonstrate a need to repatriate these funds to our U.S. operations. However, if these funds were repatriated, the amount remitted would be subject to U.S. income taxes and applicable non-U.S. income and withholding taxes.

Our ability to generate cash from operations to meet our liquidity obligations could be adversely affected in the future by factors such as general economic and market conditions, lack of availability of raw material components in the supply chain, a decline in demand for our services, loss of key contract customers, unsuccessful integration of acquisitions and new operations, the ability of Kimball Electronics to generate profits, and other unforeseen circumstances. In particular, should demand for our customers' products and, in turn, our services decrease significantly over the next 12 months, the available cash provided by operations could be adversely impacted.

The preceding statements include forward-looking statements under the Private Securities Litigation Reform Act of 1995. Certain factors could cause actual results to differ materially from forward-looking statements.

Fair Value

During fiscal year 2016, no level 1 or level 2 financial instruments were affected by a lack of market liquidity. For level 1 financial assets, readily available market pricing was used to value the financial instruments. Our foreign currency derivatives, which were classified as level 2 assets/liabilities, were independently valued using observable market inputs such as forward interest rate yield curves, current spot rates, and time value calculations. To verify the reasonableness of the independently determined fair values, these derivative fair values were compared to fair values calculated by the counterparty banks. Our own credit risk and counterparty credit risk had an immaterial impact on the valuation of the foreign currency derivatives.

See Note 12 - Fair Value of Notes to Consolidated Financial Statements for more information.

Contractual Obligations

The following table summarizes the Company's contractual obligations as of June 30, 2016.

	Payments Due During Fiscal Years Ending June 30				
(Amounts in Millions)	Total	2017	2018-2019	2020-2021	Thereafter
Recorded Contractual Obligations: [a]					
Long-Term Debt Obligations [b]	$9.0	$9.0	$ —	$ —	$ —
Other Long-Term Liabilities Reflected on the Balance Sheet [c] [d] [e]	10.0	0.8	1.1	1.8	6.3
Unrecorded Contractual Obligations:					
Operating Leases [e]	2.7	0.3	0.6	0.6	1.2
Purchase Obligations [f]	184.7	183.4	1.3	—	—
Total	$206.4	$193.5	$ 3.0	$ 2.4	$ 7.5

(a) As of June 30, 2016, we had no Capital Lease Obligations.

(b) Amounts outstanding on our credit facilities and the accrued interest for these amounts are included on the Long-Term Debt Obligations line. Refer to Note 7 - Credit Facilities of Notes to Consolidated Financial Statements for more information regarding our credit facilities. The fiscal year 2017 amount was recorded as a current liability.

(c) The timing of payments of certain items included on the Other Long-Term Liabilities Reflected on the Balance Sheet line above is estimated based on the following assumptions:

- The timing of SERP payments is estimated based on an assumed retirement age of 62 with payout based on the prior distribution elections of participants. The fiscal year 2017 amount includes $0.2 million for SERP payments recorded as current liabilities.
- The timing of severance plan payments is estimated based on the average remaining service life of employees. The fiscal year 2017 amount includes $0.3 million for severance payments recorded as a current liability.
- The timing of warranty payments is estimated based on historical data. The fiscal year 2017 amount includes $0.3 million for short-term warranty payments recorded as a current liability.

(d) Excludes $2.1 million of long-term unrecognized tax benefits and associated accrued interest and penalties along with deferred tax liabilities which are not tied to a contractual obligation and for which we cannot make a reasonably reliable estimate of the period of future payments.

(e) Refer to Note 6 - Commitments and Contingent Liabilities of Notes to Consolidated Financial Statements for more information regarding Operating Leases and certain Other Long-Term Liabilities.

(f) Purchase Obligations are defined as agreements to purchase goods or services that are enforceable and legally binding and that specify all significant terms. The amounts listed above for purchase obligations include contractual commitments for items such as raw materials, supplies, capital expenditures, services, and software acquisitions/license commitments. Cancellable purchase obligations that we intend to fulfill are also included in the purchase obligations amount listed. In certain instances, such as when lead times dictate, we enter into contractual agreements for material in excess of the levels required to fulfill customer orders. In turn, agreements with the customers cover a portion of that exposure for the material which was purchased prior to having a firm order.

Off-Balance Sheet Arrangements

In limited circumstances, we receive banker's acceptance drafts from customers in our China operation. In turn, we may transfer the acceptance drafts to a supplier in settlement of current accounts payable. These drafts contain certain recourse provisions afforded to the transferee under laws of the People's Republic of China, and if exercised, our China operation would be required to satisfy the obligation with the transferee and the draft would revert back to our China operation. At June 30, 2016, the drafts transferred and outstanding totaled $2.7 million. No transferee has exercised their recourse rights against us.

We also have standby letters of credit and operating leases entered into in the normal course of business. These arrangements do not have a material current effect and are not reasonably likely to have a material future effect on our financial condition, results of operations, liquidity, capital expenditures, or capital resources.

See Note 1 - Business Description and Summary of Significant Accounting Policies of Notes to Consolidated Financial Statements for more information on the banker's acceptance drafts and Note 6 - Commitments and Contingent Liabilities of Notes to Consolidated Financial Statements for more information on standby letters of credit. We do not have material exposures to trading activities of non-exchange traded contracts.

Critical Accounting Policies

Kimball Electronics' Consolidated Financial Statements have been prepared in accordance with accounting principles generally accepted in the United States of America. These principles require the use of estimates and assumptions that affect amounts reported and disclosed in the Consolidated Financial Statements and related notes. Actual results could differ from these estimates and assumptions. Management uses its best judgment in the assumptions used to value these estimates, which are based on current facts and circumstances, prior experience, and other assumptions that are believed to be reasonable. Management believes the following critical accounting policies reflect the more significant judgments and estimates used in preparation of our Consolidated Financial Statements and are the policies that are most critical in the portrayal of our financial position and results of operations. Management has discussed these critical accounting policies and estimates with the Audit Committee of the Company's Board of Directors and with the Company's independent registered public accounting firm.

Revenue recognition - Kimball Electronics recognizes revenue when persuasive evidence of an arrangement exists, delivery has occurred, the sales price is fixed or determinable, and collectability is reasonably assured. Delivery is not considered to have occurred until the title and the risk of loss passes to the customer according to the terms of the contract. Title and risk of loss are transferred upon shipment to or receipt at our customers' locations, or in limited circumstances, as determined by other specific sales terms of the transaction. Shipping and handling fees billed to customers are recorded as sales while the related shipping and handling costs are included in cost of sales. We recognize sales net of applicable sales tax.

Sales returns and allowances - Based on estimated product returns and price concessions, a reserve for returns and allowances is recorded at the time of the sale, resulting in a reduction of revenue. These estimates may change over time causing the provisions to be adjusted accordingly. At June 30, 2016 and June 30, 2015, the reserve for returns and allowances was \$0.2 million and \$0.3 million, respectively. This reserve was less than 0.5% of gross trade receivables during fiscal years 2016 and 2015.

Excess and obsolete inventory - Inventories were valued at lower of first-in, first-out (FIFO) cost or market value. Inventories recorded on our balance sheet are adjusted for excess and obsolete inventory. In general, we purchase materials and finished goods for contract-based business from customer orders and projections, primarily in the case of long lead time items, and we have a general philosophy to only purchase materials to the extent covered by a written commitment from our customers.

However, there are times when inventory is purchased beyond customer commitments due to minimum lot sizes and inventory lead time requirements, or where component allocation or other procurement issues may exist. We may also purchase additional inventory to support transfers of production between manufacturing facilities. Evaluation of excess inventory includes such factors as anticipated usage, inventory turnover, inventory levels, and product demand levels. Factors considered when evaluating inventory obsolescence include the age of on-hand inventory and reduction in value due to damage, design changes, or cessation of product lines. When we estimate that the current market value is below cost or determine that future demand is lower than current inventory levels, based on our evaluation of the above factors or other relevant current and projected factors associated with current economic conditions, a reduction in inventory cost to estimated net realizable value will be recorded as expense in Cost of Sales.

Self-insurance reserves - We are self-insured up to certain limits for general liability, workers' compensation, and certain employee health benefits such as medical, short-term disability, and dental with the related liabilities included in the accompanying financial statements. Our policy is to estimate reserves based upon a number of factors including known claims, estimated incurred but not reported claims, and other analyses, which are based on historical information along with certain assumptions about future events. Changes in assumptions for such matters as increased medical costs and changes in actual experience could cause these estimates to change and reserve levels to be adjusted accordingly. At June 30, 2016 and June 30, 2015, accrued liabilities for self-insurance exposure were \$1.1 million and \$0.7 million, respectively.

Taxes - Deferred income tax assets and liabilities are recognized for the estimated future tax consequences attributable to temporary differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. These assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which the temporary differences are expected to reverse. We evaluate the recoverability of our deferred tax assets each quarter by assessing the likelihood of future taxable income and available tax planning strategies that could be implemented to realize our deferred tax assets. If recovery is not likely, we provide a valuation allowance based on our best estimate of future taxable income in the various taxing jurisdictions and the amount of deferred taxes ultimately realizable. Future events could change management’s assessment.

We operate within multiple taxing jurisdictions and are subject to tax audits in these jurisdictions. These audits can involve complex issues, which may require an extended period of time to resolve. However, we believe we have made adequate provision for income and other taxes for all years that are subject to audit. As tax positions are effectively settled, the tax provision will be adjusted accordingly. The liability for uncertain income tax and other tax positions, including accrued interest and penalties on those positions, was $0.1 million at June 30, 2016 and less than $0.1 million at June 30, 2015.

New Accounting Standards

See Note 1 - Business Description and Summary of Significant Accounting Policies of Notes to Consolidated Financial Statements for information regarding New Accounting Standards.

Item 7A - Quantitative and Qualitative Disclosures About Market Risk

Foreign Exchange Rate Risk: Kimball Electronics operates internationally and thus is subject to potentially adverse movements in foreign currency rate changes. Our risk management strategy includes the use of derivative financial instruments to hedge certain foreign currency exposures. Derivatives are used only to manage underlying exposures and are not used in a speculative manner. Further information on derivative financial instruments is provided in Note 13 - Derivative Instruments of Notes to Consolidated Financial Statements. We estimate that a hypothetical 10% adverse change in foreign currency exchange rates from levels at June 30, 2016 and 2015 relative to non-functional currency balances of monetary instruments, to the extent not hedged by derivative instruments, would not have a material impact on profitability in an annual period.

Item 8 - Financial Statements and Supplementary Data

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

MANAGEMENT’S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

The management of Kimball Electronics, Inc. is responsible for establishing and maintaining adequate internal control over financial reporting and for the preparation and integrity of the accompanying financial statements and other related information in this report. The consolidated financial statements of the Company and its subsidiaries, including the footnotes, were prepared in accordance with accounting principles generally accepted in the United States of America and include judgments and estimates, which in the opinion of management are applied on an appropriately conservative basis. We maintain a system of internal and disclosure controls intended to provide reasonable assurance that assets are safeguarded from loss or material misuse, transactions are authorized and recorded properly, and that the accounting records may be relied upon for the preparation of the financial statements. This system is tested and evaluated regularly for adherence and effectiveness by employees who work within the internal control processes and by our staff of internal auditors.

The Audit Committee of the Board of Directors, which is comprised of directors who are not employees of the Company, meets regularly with management, our internal auditors, and the independent registered public accounting firm to review our financial policies and procedures, our internal control structure, the objectivity of our financial reporting, and the independence of the independent registered public accounting firm. The internal auditors and the independent registered public accounting firm have free and direct access to the Audit Committee, and they meet periodically, without management present, to discuss appropriate matters.

Because of inherent limitations, a system of internal control over financial reporting may not prevent or detect misstatements and even when determined to be effective, can only provide reasonable assurance with respect to financial statement preparation and presentation.

These consolidated financial statements are subject to an evaluation of internal control over financial reporting conducted under the supervision and with the participation of management, including the Chief Executive Officer and Chief Financial Officer. Based on that evaluation, conducted under the criteria established in Internal Control — Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission, management concluded that our internal control over financial reporting was effective as of June 30, 2016.

/s/ DONALD D. CHARRON
Donald D. Charron
Chairman of the Board,
Chief Executive Officer
August 25, 2016

/s/ MICHAEL K. SERGESKETTER
Michael K. Sergesketter
Vice President,
Chief Financial Officer
August 25, 2016

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Share Owners of
Kimball Electronics, Inc.
Jasper, Indiana

We have audited the accompanying consolidated balance sheets of Kimball Electronics, Inc. and subsidiaries (the "Company") as of June 30, 2016 and 2015, and the related consolidated statements of income, comprehensive income, share owners' equity, and cash flows for each of the three years in the period ended June 30, 2016. Our audits also included the financial statement schedule listed in the Index at Item 15. These financial statements and financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on the financial statements and financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the Company as of June 30, 2016 and 2015, and the results of its operations and its cash flows for each of the three years in the period ended June 30, 2016, in conformity with accounting principles generally accepted in the United States of America. Also, in our opinion, such financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

/s/ Deloitte & Touche LLP
DELOITTE & TOUCHE LLP
Indianapolis, Indiana
August 25, 2016

KIMBALL ELECTRONICS, INC.
CONSOLIDATED BALANCE SHEETS
(Amounts in Thousands, Except for Share Data)

	June 30, 2016	June 30, 2015
ASSETS		
Current Assets:		
Cash and cash equivalents	$54,738	$65,180
Receivables, net of allowances of $192 and $236, respectively	149,652	139,892
Inventories	132,877	125,198
Prepaid expenses and other current assets	24,944	23,922
Total current assets	362,211	354,192
Property and Equipment, net of accumulated depreciation of $161,034 and $151,504, respectively	120,701	106,779
Goodwill	6,191	2,564
Other Intangible Assets, net of accumulated amortization of $25,817 and $24,952, respectively	4,593	4,509
Other Assets	16,869	15,213
Total Assets	$510,565	$483,257
LIABILITIES AND SHARE OWNERS' EQUITY		
Current Liabilities:		
Borrowings under credit facilities	$9,000	$—
Accounts payable	142,152	133,409
Accrued expenses	23,651	26,545
Total current liabilities	174,803	159,954
Other long-term liabilities	11,393	10,854
Total Liabilities	186,196	170,808
Share Owners' Equity:		
Preferred stock-no par value Shares authorized: 15,000,000 Shares issued: none	—	—
Common stock-no par value Shares authorized: 150,000,000 Shares issued: 29,430,000 and 29,172,000, respectively	—	—
Additional paid-in capital	301,581	298,491
Retained earnings	48,492	26,205
Accumulated other comprehensive income (loss)	(12,190)	(12,247)
Treasury stock, at cost: Shares: 1,210,000 and none, respectively	(13,514)	—
Total Share Owners' Equity	324,369	312,449
Total Liabilities and Share Owners' Equity	$510,565	$483,257

See Notes to Consolidated Financial Statements

KIMBALL ELECTRONICS, INC.
CONSOLIDATED STATEMENTS OF INCOME
(Amounts in Thousands, Except for Per Share Data)

	Year Ended June 30		
	2016	2015	2014
Net Sales	$842,060	$819,350	$741,530
Cost of Sales	777,522	746,927	680,534
Gross Profit	64,538	72,423	60,996
Selling and Administrative Expenses	34,816	36,068	36,352
Other General Income	—	—	(5,688)
Restructuring Expense	—	—	402
Operating Income	29,722	36,355	29,930
Other Income (Expense):			
Interest income	79	36	41
Interest expense	(80)	(11)	(2)
Non-operating income	166	227	722
Non-operating expense	(1,911)	(1,836)	(449)
Other income (expense), net	(1,746)	(1,584)	312
Income Before Taxes on Income	27,976	34,771	30,242
Provision for Income Taxes	5,689	8,566	5,629
Net Income	$22,287	$26,205	$24,613
Earnings Per Share of Common Stock:			
Basic	$0.77	$0.90	$0.84
Diluted	$0.76	$0.89	$0.84
Average Number of Shares Outstanding:			
Basic	28,916	29,162	29,143
Diluted	29,176	29,388	29,143

See Notes to Consolidated Financial Statements

KIMBALL ELECTRONICS, INC.
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Amounts in Thousands)

	Year Ended June 30, 2016			Year Ended June 30, 2015			Year Ended June 30, 2014		
	Pre-tax	Tax	Net of Tax	Pre-tax	Tax	Net of Tax	Pre-tax	Tax	Net of Tax
Net Income			$22,287			$26,205			$24,613
Other Comprehensive Income (Loss):									
Foreign currency translation adjustments	$(540)	$—	$(540)	$(14,022)	$(16)	$(14,038)	$4,358	$(471)	$3,887
Postemployment severance actuarial change	507	(195)	312	638	(244)	394	(6)	4	(2)
Derivative gain (loss)	(2,869)	937	(1,932)	3,806	(227)	3,579	73	(29)	44
Reclassification to (earnings) loss:									
Derivatives	3,537	(1,185)	2,352	(4,307)	577	(3,730)	1,187	(277)	910
Amortization of prior service costs	28	(10)	18	28	(11)	17	40	(16)	24
Amortization of actuarial change	(254)	101	(153)	(146)	58	(88)	53	(21)	32
Other Comprehensive Income (Loss)	$409	$(352)	$57	$(14,003)	$137	$(13,866)	$5,705	$(810)	$4,895
Total Comprehensive Income			$22,344			$12,339			$29,508

See Notes to Consolidated Financial Statements

KIMBALL ELECTRONICS, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Amounts in Thousands)

	Year Ended June 30		
	2016	2015	2014
Cash Flows From Operating Activities:			
Net income	$22,287	$26,205	$24,613
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	19,869	19,607	17,889
(Gain) loss on sales of assets	(145)	(33)	10
Restructuring	—	—	311
Deferred income tax and other deferred charges	1,449	1,100	1,246
Deferred tax valuation allowance	—	(92)	(1,521)
Stock-based compensation	3,406	3,506	3,298
Excess tax benefits from stock-based compensation	(203)	—	—
Other, net	137	276	(183)
Change in operating assets and liabilities:			
Receivables	(9,192)	(14,731)	(10,076)
Inventories	(3,513)	(12,192)	(12,783)
Prepaid expenses and other current assets	(3,713)	(4,640)	(1,073)
Accounts payable	8,270	13,641	9,486
Accrued expenses	(1,820)	(4,583)	8,089
Net cash provided by operating activities	36,832	28,064	39,306
Cash Flows From Investing Activities:			
Capital expenditures	(33,664)	(33,042)	(20,404)
Proceeds from sales of assets	209	310	254
Payments for acquisitions	(8,267)	—	—
Purchases of capitalized software	(968)	(3,851)	(378)
Other, net	100	67	537
Net cash used for investing activities	(42,590)	(36,516)	(19,991)
Cash Flows From Financing Activities:			
Proceeds from revolving credit facilities	12,000	—	—
Payments on revolving credit facilities	(3,000)	—	—
Excess tax benefits from stock-based compensation	203	—	—
Repurchases of common stock	(12,606)	—	—
Repurchase of employee shares for tax withholding	(897)	—	—
Net transfers from (to) Kimball International, Inc.	—	50,295	(11,620)
Debt issuance costs	—	(123)	—
Net cash (used for) provided by financing activities	(4,300)	50,172	(11,620)
Effect of Exchange Rate Change on Cash and Cash Equivalents	(384)	(2,800)	141
Net (Decrease) Increase in Cash and Cash Equivalents	(10,442)	38,920	7,836
Cash and Cash Equivalents at Beginning of Year	65,180	26,260	18,424
Cash and Cash Equivalents at End of Year	$54,738	$65,180	$26,260

See Notes to Consolidated Financial Statements

KIMBALL ELECTRONICS, INC.
CONSOLIDATED STATEMENTS OF SHARE OWNERS' EQUITY
(Amounts in Thousands, Except for Share Data)

	Additional Paid-In Capital	Net Parent Investment	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Treasury Stock	Total Share Owners' Equity
Amounts at June 30, 2013	$—	$234,462	$—	$ (3,276)	$ —	$231,186
Net income		24,613				24,613
Other comprehensive income				4,895		4,895
Net distribution to Parent		(8,322)				(8,322)
Amounts at June 30, 2014	$—	$250,753	$—	$ 1,619	$ —	$252,372
Conversion of net Parent investment	250,753	(250,753)				—
Net income			26,205			26,205
Other comprehensive loss				(13,866)		(13,866)
Net contribution from Parent	45,973					45,973
Issuance of non-restricted stock (29,000 shares)	309					309
Compensation expense related to stock compensation plans	1,456					1,456
Amounts at June 30, 2015	$298,491	$—	$26,205	$ (12,247)	$ —	$312,449
Net income			22,287			22,287
Other comprehensive income				57		57
Issuance of non-restricted stock (47,000 shares)	(28)				545	517
Compensation expense related to stock compensation plans	2,915					2,915
Performance share issuance (258,000 shares)	203					203
Repurchase of employee shares for tax withholding (78,000 shares)					(897)	(897)
Repurchase of Common Stock (1,179,000 shares)						