

LGL GROUP INC
Form 10-K
March 29, 2016
UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-K

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

For the fiscal year ended: December 31, 2015

OR

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: 1-106

The LGL Group, Inc.

(Exact name of Registrant as Specified in Its Charter)

Delaware 38-1799862
(State or Other Jurisdiction of (I.R.S. Employer
Incorporation or Organization) Identification No.)

2525 Shader Road, Orlando, Florida 32804
(Address of Principal Executive Offices) (Zip Code)

Registrant's telephone number, including area code: (407) 298-2000

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

Title of each class	Name of each exchange on which registered
Common Stock, \$0.01 Par Value	NYSE MKT

Securities registered pursuant to Section 12(g) of the Act: Warrants to purchase Common Stock (expiring August 6, 2018)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.
Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes No

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Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act).

Yes No

The aggregate market value of the registrant's voting and non-voting common equity held by non-affiliates of the registrant, based upon the closing price of the registrant's common stock on the last business day of the registrant's most recently completed second fiscal quarter of \$4.41, was \$9,610,493. Solely for the purpose of this calculation, shares held by directors and executive officers of the registrant have been excluded. Such exclusion should not be deemed a determination or an admission by the registrant that such individuals are, in fact, affiliates of the registrant. The number of outstanding shares of the registrant's common stock was 2,665,434 as of March 23, 2015.

THE LGL GROUP, INC.

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PART I

Caution Concerning Forward-Looking Statements

This annual report on Form 10-K (this "Report") and the Company's other communications and statements may contain "forward-looking statements," including statements about the Company's beliefs, plans, objectives, goals, expectations, estimates, projections and intentions. These statements are subject to significant risks and uncertainties and are subject to change based on various factors, many of which are beyond the Company's control. The words "may," "could," "should," "would," "believe," "anticipate," "estimate," "expect," "intend," "plan," "target," "goal," and similar expressions are intended to identify forward-looking statements. All forward-looking statements, by their nature, are subject to risks and uncertainties. The Company's actual future results may differ materially from those set forth in the Company's forward-looking statements. For information concerning these factors and related matters, see "Risk Factors" in Part I, Item 1A in this Report, and "Management's Discussion and Analysis of Financial Condition and Results of Operations" in Part II, Item 7 in this Report. However, other factors besides those referenced could adversely affect the Company's results, and you should not consider any such list of factors to be a complete set of all potential risks or uncertainties. Any forward-looking statements made by the Company herein speak as of the date of this Report. The Company does not undertake to update any forward-looking statement, except as required by law. As a result, you should not place undue reliance on these forward-looking statements.

Item 1. Business.

The LGL Group, Inc. (together with its subsidiaries, the "Company" or "LGL") is a globally-positioned producer of industrial and commercial products and services that is currently focused on the design and manufacture of highly-engineered, high reliability frequency and spectrum control products. These electronic components ensure reliability and security in aerospace and defense communications, low noise and base accuracy for laboratory instruments, and synchronous data transfers throughout the wireless and Internet infrastructure. The Company was incorporated in 1928 under the laws of the State of Indiana, and in 2007, the Company was reincorporated under the laws of the State of Delaware as The LGL Group, Inc. LGL maintains its executive offices at 2525 Shader Road, Orlando, Florida, 32804. The Company's telephone number is (407) 298-2000. The Company's common stock is traded on the NYSE MKT under the symbol "LGL." The Company's warrants to purchase common stock, expiring August 6, 2018, are available for trading on the over-the-counter market under the symbol "LGLPW."

The Company operates through its principal subsidiary, M-tron Industries, Inc. (together with its subsidiaries, "MtronPTI"), which has design and manufacturing facilities in Orlando, Florida, Yankton, South Dakota and Noida, India, as well as local sales and customer support offices in Sacramento, California and Hong Kong.

Overview of MtronPTI

Originally founded in 1965, MtronPTI designs, manufactures and markets highly-engineered, high reliability frequency and spectrum control products. These component-level devices are used extensively in infrastructure equipment for the telecommunications and network equipment industries, as well as in electronic systems for applications in defense, aerospace, earth-orbiting satellites, down-hole drilling, medical devices, instrumentation, industrial devices and global positioning systems.

As an engineering-centric company, MtronPTI provides close support to the customer throughout their products' entire life cycle, including product design, prototyping, production, and subsequent product upgrades. This collaborative approach has resulted in the development of long-standing business relationships with its blue-chip customer base.

MtronPTI's Strategy

MtronPTI's primary objective is to create long-term growth with a market-based approach of designing and bringing new products to its customers through both organic research and development, and through strategic partnerships, joint ventures, acquisitions or mergers. Through direct collaboration with original equipment manufacturers ("OEMs"), our customers, MtronPTI seeks to leverage its core strength as an engineering leader to expand client access, add new capabilities and continue to diversify its product offerings. MtronPTI's focus is on investments that will differentiate and broaden its RF/microwave portfolio and lead toward higher levels of integration. We believe that successful execution of this strategy will lead to a transformation of MtronPTI's product portfolio towards longer product life cycles, better margins and improved competitive position.

Products

MtronPTI's portfolio is divided into two product groupings, Frequency Control and Spectrum Control, and has expanded from primarily crystal-based components to include higher levels of integration, advanced materials science, cavity-based products, and various types of compensation methods employing integrated circuits and other methods. These products are differentiated by their precise level of accuracy, their stability over time and within harsh environments, and their very low phase noise.

MtronPTI's Frequency Control product group includes a broad portfolio of XTAL, clock oscillators, VCXO, TCXO OCXO and DOCXO devices which meet some of the tightest specifications, including IEEE 1588 standards. These devices may be based on quartz, quartz MEMS, or advanced materials science designed to achieve higher performance levels than quartz. MtronPTI's products offer high reliability over a wide temperature range and are well-suited for harsh environments, including shock and vibration-resistant oscillators with low-g sensitivity. These products are designed for applications within aerospace and defense, telecommunications infrastructure and instrumentation markets.

MtronPTI's Spectrum Control product group includes a wide array of RF, microwave and millimeter wave filters and diplexers covering a frequency range from 1 MHz to 90 GHz, and solid state power amplifiers covering a frequency range from 300 MHz to 26 GHz, with power output from 10 Watts to 10 kWatts. Filter devices include crystal, ceramic, LC, tubular, combline, cavity, interdigital and metal insert waveguide, as well as digital, analog and mechanical tunable filters, switched filter arrays and RF subsystems. Power amplifiers add active devices to MtronPTI's portfolio and include GaN, GaAS FET, LDMOS and chip and wire technologies in narrow or broadband, module or rack-mounted packages. These products are employed in applications within the aerospace, defense and commercial markets.

As always, new product development is a key focus for MtronPTI as it continues to push its roadmap to meet the needs of its served markets. Within Frequency Control, design efforts are focused on smaller packages, lower power, and use of new materials to provide compensation and harsh environment performance that surpasses customer requirements. Spectrum Control seeks to develop higher power handling, higher levels of integration and a range of integrated products within the RF subsystem.

Manufacturing and Operations

MtronPTI has design and manufacturing facilities located in Orlando, Florida, Yankton, South Dakota and Noida, India, providing nearly 120,000 square feet of manufacturing space on approximately 14 acres of land. All of its production facilities are ISO 9001:2008 certified, ITAR registered and RoHS compliant. In addition, its U.S. production facilities in Orlando and Yankton are AS9100 Rev C and MIL-STD-790 certified.

MtronPTI's headquarters are located in Orlando, Florida, with sales and customer support offices also located in Sacramento, California and Hong Kong.

Research and Development

Utilizing its understanding of market requirements, MtronPTI employs a disciplined approach to capital allocation when selecting new product development projects. A cross-functional team comprised of engineering, marketing, operations, sales and finance reviews the merits of specific projects, seeking to invest in products that will exceed a specific return on investment level and a payback expectation within one to two years. In addition, the team considers the inherent value of intellectual property that each project presents with consideration for technical roadmap objectives.

Research and development expense was approximately \$1,964,000 and \$2,166,000 in 2015 and 2014, respectively, and will remain a significant part of MtronPTI's efforts to revitalize its IP position.

Customers

MtronPTI primarily works directly with OEMs to define the right solutions for their unique applications, including the design of custom parts with unique part numbers. Actual sales of production parts may be directly to the OEM or through either their designated contract manufacturers ("CMs"), or through franchised distributors of MtronPTI's products. As a result, MtronPTI has highly-skilled sales engineers who work directly with the designers and program managers at its OEMs, providing a high-level of engineering support at all points within the process. Over MtronPTI's 50-year history, it has developed a long list of blue-chip customers that have come to rely on its products because of their performance characteristics and their reliability.

In 2015, MtronPTI's largest customer, an electronics contract manufacturing company in the aerospace and defense markets, accounted for \$2,627,000, or 12.7%, of the Company's total revenues, compared to \$2,522,000, or 11.0%, in 2014.

Marketing and Sales

MtronPTI has a highly skilled team of sales engineers who work in tandem with a worldwide network of more than 30 independent external manufacturer representatives and franchised electronics distributors to market and sell its products. An important part of the sales process is gaining qualification of specific products from the OEM, confirming suitability for use in a specific system design, which is commonly referred to as a "design-win." Through direct contact with its clients and through its representative network, MtronPTI is able to understand the needs of the marketplace and then guide its product development process to allocate resources to meeting those requirements.

Seasonality

MtronPTI's business is not seasonal, although shipment schedules may be affected by the production schedules of its customers or their CMs based on regional practices or customs.

Domestic Revenues

MtronPTI's domestic revenues were \$15,260,000 in 2015, or 73.7% of total consolidated revenues, compared to \$13,556,000, or 58.9% of total consolidated revenues, in 2014.

International Revenues

MtronPTI's international revenues were \$5,453,000 in 2015, or 26.3% of total consolidated revenues, compared to \$9,457,000, or 41.1% of total consolidated revenues, in 2014. In each of 2015 and 2014, these revenues were derived mainly from customers in Asia, with significant sales in Malaysia and China. MtronPTI avoids significant currency exchange risk by transacting and settling substantially all international sales in United States dollars.

Order Backlog

MtronPTI's order backlog was \$8,799,000 and \$8,792,000 as of December 31, 2015 and 2014, respectively. The backlog of unfilled orders includes amounts based on signed contracts as well as agreed letters of intent, which MtronPTI has determined are firm orders and likely to proceed. Although backlog represents only firm orders that are considered likely to be fulfilled within the 12 months following receipt of the order, cancellations or scope adjustments may and do occur.

Order backlog is adjusted quarterly to reflect project cancellations, deferrals, revised project scope and cost. The Company expects to fill its entire 2015 order backlog in 2016, but cannot provide assurances as to what portion of the order backlog will be fulfilled in a given year.

Raw Materials

Most raw materials used in the production of MtronPTI products are available in adequate supply from a number of sources and the prices of these raw materials are relatively stable. However, some raw materials, including printed circuit boards, quartz and certain metals including steel, aluminum, silver, gold, tantalum and palladium, are subject to greater supply fluctuations and price volatility, as experienced in recent years. MtronPTI generally has been able to include some cost increases in its pricing, but in some cases its margins were adversely impacted.

Competition

Production of frequency and spectrum control devices is a highly competitive industry, with low transportation costs and few import barriers. There are numerous domestic and international manufacturers who are capable of providing custom-designed timing and filter products comparable in quality and performance to MtronPTI's products.

Competitors include, but are not limited to, Vectron International (a division of Knowles Corporation), K&L Microwave (a division of Dover Corporation), CTS Corporation, and Rakon Limited. MtronPTI's competitive strategy begins with its focus on manufacturing lower volumes of more precise, custom designed frequency control devices, rather than producing higher volumes of standardized products like some of its competitors. MtronPTI also seeks to outperform the competition by producing market-based design solutions for customers utilizing MtronPTI's technical skill, and its high-performance, high-reliability product portfolio, and by providing high level quality engineering support throughout the customer's design process and the entire life cycle of the product.

Intellectual Property

MtronPTI has no patents, trademarks or licenses that are considered to be significant to its business or operations.

Rather, MtronPTI believes that its technological position depends primarily on the technical competence and creative ability of its engineering and technical staff in areas of product design and manufacturing processes, including their ability to customize to meet difficult specifications, as well as proprietary know-how and information.

Employees

As of December 31, 2015, the Company employed 141 people (full-time equivalents): two within corporate headquarters and 139 within its subsidiary, MtronPTI, which includes 33 in Yankton, South Dakota, 95 in Orlando, Florida, three in Hong Kong and eight in Noida, India. None of the Company's employees are represented by a labor union and the Company considers its relationships with employees to be good.

As an engineering-centric company, nearly 20% of MtronPTI's workforce consists of degreed-engineers bringing their expertise to product design and process development.

Environmental

The Company's manufacturing operations, products, and/or product packaging are subject to environmental laws and regulations governing air emissions, wastewater discharges, and the handling, disposal and remediation of hazardous substances, wastes and other chemicals. In addition, more stringent environmental regulations may be enacted in the future, both within the United States and internationally, and we cannot presently determine the modifications, if any, in the Company's operations that any future regulations might require, or the cost of compliance that would be associated with these regulations.

To date, capital expenditures, earnings and competitive position of the Company have not been materially affected by compliance with current federal, state, and local laws and regulations (domestic and foreign) relating to the protection of the environment. However, the Company cannot predict the effect of future laws and regulations.

Item 1A. Risk Factors.

Investing in our securities involves risks. Before making an investment decision, you should carefully consider the risks described below. Any of these risks could result in a material adverse effect on our business, financial condition, results of operations, or prospects, and could cause the trading price of our securities to decline, resulting in a loss of all or part of your investment.

Risks Related to Our Business and Industry

We are dependent on a single line of business.

We are currently engaged in the design, manufacture and marketing of standard and custom-engineered electronic components that are used primarily to control the frequency or timing of signals in electronic circuits, and we do not offer any other products. Virtually all of MtronPTI's 2015 and 2014 revenues came from sales of electronic components, which consist of packaged quartz crystals, oscillator modules, electronic filters and integrated modules. We expect that this product line will continue to account for substantially all of MtronPTI's revenues in 2016.

Given our reliance on this single line of business, any decline in demand for this product line or failure to achieve continued market acceptance of existing and new versions of this product line may harm MtronPTI's business and our financial condition. Additionally, unfavorable market conditions affecting this line of business would likely have a disproportionate impact on us in comparison with certain competitors, who have more diversified operations and multiple lines of business. Should this line of business fail to generate sufficient sales to support ongoing operations, there can be no assurance that we will be able to develop alternate business lines.

Our operating results vary significantly from period to period.

We experience fluctuations in our operating results. Some of the principal factors that contribute to these fluctuations include: changes in demand for our products; our effectiveness in managing manufacturing processes, costs and inventory; our effectiveness in engineering and qualifying new product designs with our OEM customers and in managing the risks associated with bringing those new products into production; changes in the cost and availability of raw materials, which often occur in the electronics manufacturing industry and which affect our margins and our ability to meet delivery schedules; macroeconomic and served industry conditions; and events that may affect our production capabilities, such as labor conditions and political instability. In addition, due to the prevailing economic climate and competitive differences between the various market segments which we serve, the mix of sales between our communications, networking, aerospace, defense, industrial and instrumentation market segments may affect our operating results from period to period.

For the years ended December 31, 2015 and 2014, we had net losses of approximately (\$711,000) and (\$2,825,000), respectively. Our revenues are derived solely from our operating subsidiary, MtronPTI, and its future rate of growth and profitability are highly dependent on the development and growth of demand for our products in the communications, networking, aerospace, defense, instrumentation and industrial markets, which are cyclical. We cannot be certain whether we will generate sufficient revenues or sufficiently manage expenses to return to profitability.

We have a large customer that accounts for a significant portion of our revenues, and the loss of this customer, or decrease in their demand for our products, could have a material adverse effect on our results.

In 2015, MtronPTI's largest customer, an electronics contract manufacturing company, accounted for \$2,627,000, or 12.7%, of the Company's total revenues, compared to \$2,522,000, or 11.0%, in 2014. The loss of this customer, or a decrease in their demand for our products, could have a material adverse effect on our results.

A relatively small number of customers account for a significant portion of our accounts receivable, and the insolvency of any of these customers could have a material adverse impact on our liquidity.

At December 31, 2015, three of MtronPTI's largest customers accounted for approximately \$819,000, or 31.4%, of accounts receivable, compared to approximately \$1,035,000, or 31.3%, at the end of 2014. The insolvency of any of these customers could have a material adverse impact on our liquidity.

MtronPTI's order backlog may not be indicative of future revenues.

MtronPTI's order backlog comprises orders that are subject to specific production release, orders under written contracts, oral and written orders from customers with which MtronPTI has had long-standing relationships and written purchase orders from sales representatives. MtronPTI's customers may order components from multiple sources to ensure timely delivery when backlog is particularly long and may cancel or defer orders without significant penalty. They also may cancel orders when business is weak and inventories are excessive. As a result, the Company cannot provide assurances as to the portion of backlog orders to be filled in a given year, and MtronPTI's order backlog as of any particular date may not be representative of actual revenues for any subsequent period.

We are a holding company, and therefore are dependent upon the operations of our subsidiaries to meet our obligations.

We are a holding company that transacts business through our operating subsidiaries. Our primary assets are the shares of our operating subsidiaries. Our ability to meet our operating requirements and to make other payments depends on the surplus and earnings of our subsidiaries and their ability to pay dividends or to advance or repay funds.

MtronPTI's future rate of growth and profitability are highly dependent on the development and growth of the communications, networking, aerospace, defense, instrumentation and industrial markets, which are cyclical.

In 2015 and 2014, the majority of MtronPTI's revenues were derived from sales to manufacturers of equipment for the communications, networking, defense, aerospace, instrumentation and industrial markets for frequency and spectrum control devices, including indirect sales through distributors and contract manufacturers. During 2016, MtronPTI expects a significant portion of its revenues to continue to be derived from sales to these manufacturers. Often OEMs and other service providers within these markets have experienced periods of capacity shortage and periods of excess capacity, as well as periods of either high or low demand for their products. In periods of excess capacity or low demand, purchases of capital equipment may be curtailed, including equipment that incorporates MtronPTI's products. A reduction in demand for the manufacture and purchase of equipment for these markets, whether due to cyclical, macroeconomic or other factors, or due to MtronPTI's reduced ability to compete based on cost or technical factors, could substantially reduce MtronPTI's net sales and operating results and adversely affect its financial condition. Moreover, if these markets fail to grow as expected, MtronPTI may be unable to maintain or grow its revenue.

The multiple variables which affect the communications, networking, aerospace, defense, instrumentation and industrial markets for equipment that require frequency and spectrum control devices, as well as the number of parties involved in the supply chain and manufacturing process, can impact inventory levels and lead to supply chain inefficiencies. As a result of these complexities, MtronPTI has limited visibility to forecast revenue projections accurately for the near and medium-term timeframes.

The market share of our customers in the communications, networking, aerospace, defense, instrumentation and industrial markets may change over time, reducing the potential value of our relationships with our existing customer base.

We have developed long-term relationships with our existing customers, including pricing contracts, custom designs and approved vendor status. If these customers lose market share to other equipment manufacturers in the communications, networking, aerospace, defense, instrumentation and industrial markets with whom we do not have similar relationships, our ability to maintain revenue, margin or operating performance may be adversely affected. We may make acquisitions that are not successful, or we may fail to integrate acquired businesses into our operations properly.

We intend to explore opportunities to buy other businesses or technologies that could complement, enhance or expand our current business or product lines, or that might otherwise offer us growth opportunities. We may have difficulty finding such opportunities or, if such opportunities are identified, we may not be able to complete such transactions for reasons including a failure to secure necessary financing.

Any transactions that we are able to identify and complete may involve a number of risks, including:

The diversion of our management's attention from the management of our existing business to the integration of the operations and personnel of the acquired or combined business or joint venture;

Due diligence may not identify material business risks;

Possible adverse effects on our operating results during the integration process;

Substantial acquisition-related expenses, which would reduce our net income, if any, in future years;

The loss of key employees and customers as a result of changes in management; and

Our possible inability to achieve the intended objectives of the transaction.

In addition, we may not be able to integrate, operate, maintain or manage, successfully or profitably, our newly acquired operations or employees. We may not be able to maintain uniform standards, controls, policies and procedures, and this may lead to operational inefficiencies.

Any of these difficulties could have a material adverse effect on our business, financial condition, results of operations and cash flows.

If MtronPTI is unable to introduce innovative products, demand for its products may decrease.

MtronPTI's future operating results are dependent on its ability to develop, introduce and market innovative products continually, to modify existing products, to respond to technological change and to customize some of its products to meet customer requirements. There are numerous risks inherent in this process, including the risks that MtronPTI will be unable to anticipate the direction of technological change or that it will be unable to develop and market new products and applications in a timely or cost-effective manner to satisfy customer demand.

MtronPTI's markets are highly competitive, and it may lose business to larger and better-financed competitors.

MtronPTI's markets are highly competitive worldwide, with low transportation costs and few import barriers.

MtronPTI competes principally on the basis of product quality and reliability, availability, customer service, technological innovation, timely delivery and price. Within the industry in which MtronPTI competes, competition has become increasingly concentrated and global in recent years. Many of MtronPTI's major competitors, some of which are larger, and potential competitors have substantially greater financial resources and more extensive engineering, manufacturing, marketing and customer support capabilities. If we are unable to successfully compete against current and future competitors, our operating results will be adversely affected.

Our ability to borrow under our credit facility may be limited by available collateral.

Our credit facility includes a revolving loan that requires cash equal to any amounts outstanding to be held as collateral in a deposit account with the lender. Should we not have sufficient cash to be held as collateral, the total amount available to borrow under the revolving loan may be reduced or not available.

Our success depends on our ability to retain key management and technical personnel and attracting, retaining, and training new technical personnel.

Our future growth and success will depend in large part upon our ability to recruit highly-skilled technical personnel, including engineers, and to retain our existing management and technical personnel. The labor markets in which we operate are highly competitive and some of our operations are not located in highly populated areas. As a result, we may not be able to recruit and retain key personnel. Our failure to hire, retain or adequately train key personnel could have a negative impact on our performance.

MtronPTI purchases certain key components and raw materials from single or limited sources and could lose sales if these sources fail to fulfill its needs.

If single-source components or key raw materials were to become unavailable on satisfactory terms, and MtronPTI could not obtain comparable replacement components or raw materials from other sources in a timely manner, the Company's business, results of operations and financial condition could be harmed. On occasion, one or more of the components used in MtronPTI's products have become unavailable, resulting in unanticipated redesign and related delays in shipments. We cannot give assurance that similar delays will not occur in the future. Our suppliers may be impacted by compliance with environmental regulations including Restriction of Hazardous Substances ("RoHS") and Waste Electrical and Electronic Equipment ("WEEE"), which could disrupt the supply of components or raw materials or cause additional costs for MtronPTI to implement new components or raw materials into its manufacturing process. As a supplier to U.S. Government defense contractors, we are subject to a number of procurement regulations and other requirements and could be adversely affected by changes in regulations or any negative findings from a U.S. audit or investigation.

A number of our customers are U.S. Government contractors. As one of their suppliers, we must comply with significant procurement regulations and other requirements. We also maintain registration under the International Traffic in Arms Regulations for all of our production facilities. One of those production facilities must comply with additional requirements and regulations for its production processes and for selected personnel in order to maintain the security of classified information. These requirements, although customary within these markets, increase our performance and compliance costs. If any of these various requirements change, our costs of complying with them could increase and reduce our operating margins.

We operate in a highly regulated environment and are routinely audited and reviewed by the U.S. Government and its agencies such as the Defense Contract Audit Agency ("DCAA") and Defense Contract Management Agency ("DCMA"). These agencies review our performance under our contracts, our cost structure and our compliance with applicable laws, regulations, and standards, as well as the adequacy of, and our compliance with, our internal control systems and policies. Systems that are subject to review include our purchasing systems, billing systems, property management and control systems, cost estimating systems, compensation systems and management information systems. Any costs found to be improperly allocated to a specific contract will not be reimbursed or must be refunded if already reimbursed. If an audit uncovers improper or illegal activities, we may be subject to civil and criminal penalties and administrative sanctions, which may include termination of contracts, forfeiture of profits, suspension of payments, fines and suspension, or prohibition from doing business as a supplier to contractors who sell products and services to the U.S. Government. In addition, our reputation could be adversely affected if allegations of impropriety were made against us.

From time to time, we may also be subject to U.S. Government investigations relating to our or our customers' operations and products, and are expected to perform in compliance with a vast array of federal laws, including the Truth in Negotiations Act, the False Claims Act, the International Traffic in Arms Regulations promulgated under the Arms Export Control Act, and the Foreign Corrupt Practices Act. We or our customers may be subject to reductions of the value of contracts, contract modifications or termination, and the assessment of penalties and fines, which could negatively impact our results of operations and financial condition, or result in a diminution in revenue from our customers, if we or our customers are found to have violated the law or are indicted or convicted for violations of federal laws related to government security regulations, employment practices or protection of the environment, or are found not to have acted responsibly as defined by the law. Such convictions could also result in suspension or debarment from serving as a supplier to government contractors for some period of time. Such convictions or actions could have a material adverse effect on us and our operating results. The costs of cooperating or complying with such audits or investigations may also adversely impact our financial results.

MtronPTI's products are complex and may contain errors or design flaws, which could be costly to correct.

When MtronPTI releases new products, or new versions of existing products, they may contain undetected or unresolved errors or defects. The vast majority of MtronPTI's products are custom-designed for requirements of specific OEM systems. The expected business life of these products ranges from less than one year to more than 10 years depending on the application. Some of the customizations are modest changes to existing product designs while others are major product redesigns or new product platforms.

Despite testing, errors or defects may be found in new products or upgrades after the commencement of commercial shipments. Undetected errors and design flaws have occurred in the past and could occur in the future. These errors could result in delays, loss of market acceptance and sales, diversion of development resources, damage to the Company's reputation, product liability claims and legal action by its customers and third parties, failure to attract new customers and increased service costs.

Communications and network infrastructure equipment manufacturers increasingly rely upon contract manufacturers, thereby diminishing our ability to sell our products directly to those equipment manufacturers.

There is a continuing trend among communications and network infrastructure equipment manufacturers to outsource the manufacturing of their equipment or components. As a result, MtronPTI's ability to persuade these OEMs to utilize our products in customer designs could be reduced and, in the absence of a manufacturer's specification of MtronPTI's products, the prices that MtronPTI can charge for them may be subject to greater competition.

Future changes in MtronPTI's environmental liability and compliance obligations may increase costs and decrease profitability.

MtronPTI's present and past manufacturing operations, products, and/or product packaging are subject to environmental laws and regulations governing air emissions, wastewater discharges, and the handling, disposal and remediation of hazardous substances, wastes and other chemicals. In addition, more stringent environmental regulations may be enacted in the future, and we cannot presently determine the modifications, if any, in MtronPTI's operations that any future regulations might require, or the cost of compliance that would be associated with these regulations.

Environmental laws and regulations may cause us to change our manufacturing processes, redesign some of our products, and change components to eliminate some substances in MtronPTI's products in order to be able to continue to offer them for sale.

We have significant international operations and sales to customers outside of the United States that subject us to certain business, economic and political risks.

We have office and manufacturing space in Noida, India, and a sales office in Hong Kong. Additionally, foreign revenues for 2015 and 2014 (primarily to Malaysia and China) accounted for 26.3% and 41.1% of our 2015 and 2014 consolidated revenues, respectively. We anticipate that sales to customers located outside of the United States will continue to be a significant part of our revenues for the foreseeable future. Our international operations and sales to customers outside of the United States subject our operating results and financial condition to certain business, economic, political, health, regulatory and other risks, including:

Political and economic instability in countries in which MtronPTI's products are manufactured and sold;

Expropriation or the imposition of government controls;

Sanctions or restrictions on trade imposed by the United States government;

Export license requirements;

Trade restrictions;

Currency controls or fluctuations in exchange rates;

High levels of inflation or deflation;

Greater difficulty in collecting accounts receivable and longer payment cycles;

Changes in labor conditions and difficulties in staffing and managing international operations; and

Limitations on insurance coverage against geopolitical risks, natural disasters and business operations.

Additionally, to date, very few of our international revenue and cost obligations have been denominated in foreign currencies. As a result, changes in the value of the United States dollar relative to foreign currencies may affect our competitiveness in foreign markets. We do not currently engage in foreign currency hedging activities, but may do so in the future to the extent that we incur a significant amount of foreign-currency denominated liabilities.

New regulations related to conflict minerals could adversely impact our business.

The Dodd-Frank Wall Street Reform and Consumer Protection Act contains provisions designed to improve transparency and accountability concerning the supply of certain minerals, known as "conflict minerals," originating from the Democratic Republic of Congo and adjoining countries that are believed to be benefitting armed groups. As a result, the SEC recently adopted new due diligence, disclosure and reporting requirements for companies that manufacture products that include components containing such minerals. Since we manufacture such products, we are required to comply with the new SEC rules. We expect that the compliance process will be both time-consuming and costly. Costs associated with complying with these disclosure requirements will include diligence to determine the sources of minerals used in our products and potential changes to products, processes or sources of supply as a consequence of such verification activities. The implementation of these rules could adversely affect the sourcing, supply and pricing of certain materials used in our products. Because there may be only a limited number of suppliers offering "conflict free" minerals, we cannot be sure that we will be able to obtain necessary minerals from such suppliers in sufficient quantities or at competitive prices. In addition, our supply chain is complex and we may not be able to easily verify the origins for all minerals used in our products. We may face reputational challenges with our customers and other stakeholders if our products contain minerals not determined to be conflict free or if we are unable to sufficiently verify the origins of minerals contained in the components included in our products through the due diligence procedures that we implement.

Risks Related to Our Securities

The price of our common stock has fluctuated considerably and is likely to remain volatile, in part due to the limited market for our common stock.

From January 1, 2015 through March 23, 2016, the high and low closing sales prices for our common stock were \$5.20 and \$3.21, respectively, and the average daily trading volume in our common stock during that time period was approximately 5,300 shares per day. There is a limited public market for our common stock, and we cannot provide assurances that a more active trading market will develop or be sustained. As a result of limited trading volume in our common stock, the purchase or sale of a relatively small number of shares could result in significant price fluctuations and it may be difficult for holders to sell their shares without depressing the market price for our common stock. Additionally, the market prices of our common stock may continue to fluctuate significantly in response to a number of factors, some of which are beyond our control, including the following:

- General economic conditions affecting the availability of long-term or short-term credit facilities, the purchasing and payment patterns of our customers, or the requirements imposed by our suppliers;

- Economic conditions in our industry and in the industries of our customers and suppliers;

- Changes in financial estimates or investment recommendations by securities analysts relating to our common stock;

- Market reaction to our reported financial results;

- Loss of a major customer;

- Announcements by us or our competitors of significant contracts, acquisitions, strategic partnerships, joint ventures or capital commitments; and

- Changes in key personnel.

Our warrants, expiring August 6, 2018, currently have a limited public market which may affect their value.

On August 6, 2013, we distributed warrants to purchase shares of our common stock (expiring August 6, 2018) as a dividend to holders of our common stock on July 29, 2013, the record date for the dividend. Stockholders received five warrants for each share of our common stock owned on the record date. When exercisable, 25 warrants will entitle their holder to purchase one share of our common stock at an exercise price of \$7.50 per share (subject to adjustment).

There is a limited public market for our warrants, and we cannot provide assurances that an active trading market will develop or be sustained. The warrants are quoted on the over-the-counter market under the symbol "LGLPW." Securities traded on the over-the-counter markets are typically less liquid than securities that trade on a national securities exchange, such as the NYSE MKT. Trading on the over-the-counter market may negatively affect the trading price and liquidity of the warrants and could result in larger spreads in the bid and ask prices for the warrants. Warrant holders may find it difficult to resell their warrants due to very limited trading volume.

The warrants are "European style warrants" and will only become exercisable on the earlier of (i) the expiration date, August 6, 2018, and (ii) such date that the 30-day volume weighted average price per share, or VWAP, of our common stock is greater than or equal to \$15.00. Once the warrants become exercisable, they may be exercised in accordance with the terms of the warrant agreement until their expiration at 5:00 p.m., Eastern Time, on the expiration date.