CTS CORP
Form 10-Q
April 26, 2018
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

(Mark One)
x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For The Quarterly Period Ended March 31, 2018

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: 1-4639

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

Indiana	35-0225010
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification Number)
4925 Indiana Avenue, Lisle, IL	60532
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code: 630-577-8800

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 o

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

(Do not check if 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

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of April 23, 2018: 33,018,206.

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PART I - FINANCIAL INFORMATION
Item 1. Financial Statements
CTS CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS - UNAUDITED
(In thousands of dollars, except per share amounts)

	Three Months Ended	
	March 31, 2018	March 31, 2017
Net sales	$113,530	$100,154
Cost of goods sold	75,097	65,930
Gross Margin	38,433	34,224
Selling, general and administrative expenses	17,372	15,248
Research and development expenses	6,507	6,003
Restructuring charges	1,195	777
Operating earnings	13,359	12,196
Other income (expense):		
Interest expense	(541)	(684)
Interest income	482	253
Other income, net	2,004	460
Total other income	1,945	29
Earnings before income taxes	15,304	12,225
Income tax expense	3,756	3,741
Net earnings	$11,548	$8,484
Earnings per share:		
Basic	$0.35	$0.26
Diluted	$0.34	$0.25
Basic weighted – average common shares outstanding:	32,975	32,802
Effect of dilutive securities	540	560
Diluted weighted – average common shares outstanding	33,515	33,362
Cash dividends declared per share	$0.04	$0.04

See notes to unaudited condensed consolidated financial statements.

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CTS CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME UNAUDITED
(In thousands of dollars)

	Three Months Ended	
	March 31, 2018	March 31, 2017
Net earnings	$11,548	$8,484
Other comprehensive income:		
Changes in fair market value of derivatives, net of tax	807	760
Changes in unrealized pension cost, net of tax	1,107	816
Cumulative translation adjustment, net of tax	243	88
Other comprehensive income	$2,157	$1,664
Comprehensive earnings	$13,705	$10,148

See notes to unaudited condensed consolidated financial statements.

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CTS CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In thousands of dollars)

	(Unaudited) March 31, 2018	December 31, 2017
ASSETS		
Current Assets		
Cash and cash equivalents	$ 121,383	$ 113,572
Accounts receivable, net	69,948	70,584
Inventories, net	37,941	36,596
Other current assets	13,266	12,857
Total current assets	242,538	233,609
Property, plant and equipment, net	90,685	88,247
Other Assets		
Prepaid pension asset	58,494	57,050
Goodwill	71,057	71,057
Other intangible assets, net	65,246	66,943
Deferred income taxes	18,428	20,694
Other	2,244	2,096
Total other assets	215,469	217,840
Total Assets	$ 548,692	$ 539,696
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities		
Accounts payable	51,937	49,201
Accrued payroll and benefits	8,497	11,867
Accrued liabilities	42,027	41,344
Total current liabilities	102,461	102,412
Long-term debt	74,000	76,300
Long-term pension obligations	7,148	7,201
Deferred income taxes	3,398	3,802
Other long-term obligations	5,953	6,176
Total Liabilities	192,960	195,891
Commitments and Contingencies (Note 10)		
Shareholders' Equity		
Common stock	305,722	304,777
Additional contributed capital	39,681	41,084
Retained earnings	430,388	420,160
Accumulated other comprehensive loss	(76,803)	(78,960)
Total shareholders' equity before treasury stock	698,988	687,061
Treasury stock	(343,256)	(343,256)
Total shareholders' equity	355,732	343,805
Total Liabilities and Shareholders' Equity	$ 548,692	$ 539,696

See notes to unaudited condensed consolidated financial statements.

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CTS CORPORATION AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS UNAUDITED
(In thousands of dollars)

	Three Months Ended March 31, 2018	Three Months Ended March 31, 2017
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net earnings	$11,548	$8,484
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	5,483	4,708
Pension and other post-retirement plan expense (income)	107	(417)
Stock-based compensation	923	880
Deferred income taxes	1,289	2,313
Loss on sales of fixed assets	1	2
Gain on foreign currency hedges, net of cash	(56)	—
Changes in assets and liabilities:		
Accounts receivable	1,435	7
Inventories	(788)	(2,076)
Other assets	147	(16)
Accounts payable	2,855	942
Accrued payroll and benefits	(3,596)	(5,169)
Accrued expenses	(69)	(2,280)
Income taxes payable	1,179	248
Other liabilities	(224)	2,232
Pension and other post-retirement plans	(80)	(79)
Net cash provided by operating activities	20,154	9,779
CASH FLOWS FROM INVESTING ACTIVITIES:		
Capital expenditures	(6,912)	(3,806)
Proceeds from sale of assets	—	1
Net cash used in investing activities	(6,912)	(3,805)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payments of long-term debt	(334,100)	(373,000)
Proceeds from borrowings of long-term debt	331,800	377,900
Dividends paid	(1,318)	(1,310)
Taxes paid on behalf of equity award participants	(1,423)	(1,566)
Net cash (used in) provided by financing activities	(5,041)	2,024
Effect of exchange rate changes on cash and cash equivalents	(390)	16
Net increase in cash and cash equivalents	7,811	8,014
Cash and cash equivalents at beginning of period	113,572	113,805
Cash and cash equivalents at end of period	$121,383	$121,819
Supplemental cash flow information:		
Cash paid for interest	$486	$529
Cash paid for income taxes, net	$809	$1,386

See notes to unaudited condensed consolidated financial statements.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - UNAUDITED
(in thousands except for share and per share data)
March 31, 2018
NOTE 1—Basis of Presentation

The accompanying condensed consolidated financial statements have been prepared by CTS Corporation (“CTS” "we", "our", "us" or the "Company”), without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been omitted pursuant to such rules and regulations. The unaudited condensed consolidated financial statements should be read in conjunction with the financial statements, notes thereto, and other information included in the Company’s Annual Report on Form 10 K for the year ended December 31, 2017.

The accompanying unaudited condensed consolidated financial statements reflect, in the opinion of management, all adjustments (consisting of normal recurring items) necessary for a fair statement, in all material respects, of the financial position and results of operations for the periods presented. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ materially from those estimates. The results of operations for the interim periods are not necessarily indicative of the results for the entire year.

Change in Accounting Principle

In May 2014, the Financial Accounting Standards Board issued Accounting Standards Update ("ASU") 2014-09, "Revenue from Contracts with Customers (Topic 606)". The guidance in this ASU affects any entity that either enters into contracts with customers to transfer goods or services or enters into contracts for the transfer of nonfinancial assets unless those contracts are within the scope of other standards (for example, insurance contracts or lease contracts). This guidance requires a company to recognize revenue to depict the transfer of goods or services to a customer at an amount that reflects the consideration it expects to receive in exchange for those goods or services.

Beginning in January 2018, CTS adopted the provisions of Topic 606 under the modified retrospective method, which requires a cumulative effect adjustment to the opening balance of retained earnings on the date of adoption. This approach was applied to contracts not completed as of December 31, 2017. At date of adoption, there was no significant change to our past revenue recognition practices and therefore no adjustment to the opening balance of retained earnings was required.

Subsequent Events

We have evaluated subsequent events and transactions for potential recognition or disclosure in the financial statements through the date the consolidated financial statements are issued.

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NOTE 2 – Revenue Recognition

The core principle of Topic 606 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The guidance provides a five-step process to achieve that core principle:

- Identify the contract(s) with a customer
- Identify the performance obligations
- Determine the transaction price
- Allocate the transaction price
- Recognize revenue when the performance obligations are met

We recognize revenue when the performance obligations specified in our contracts have been satisfied, after considering the impact of variable consideration and other factors that may affect the transaction price. Our contracts normally contain a single performance obligation that is fulfilled on the date of delivery based on shipping terms stipulated in the contract. We usually expect payment within 30 to 90 days from the shipping date, depending on our terms with the customer. None of our contracts as of March 31, 2018, contained a significant financing component. Differences between the amount of revenue recognized and the amount invoiced, collected from, or paid to our customers are recognized as contract assets or liabilities. Contract assets will be reviewed for impairment when events or circumstances indicate that they may not be recoverable.

To the extent the transaction price includes variable consideration, we estimate the amount of variable consideration that should be included in the transaction price utilizing the most likely amount method based on an analysis of historical experience and current facts and circumstances, which requires significant judgment. Variable consideration is included in the transaction price if, in our judgment, it is probable that a significant future reversal of cumulative revenue under the contract will not occur.

Contract Assets and Liabilities

Contract assets and liabilities included in our Condensed Consolidated Balance Sheets are as follows:

	As of March 31, 2018	December 31, 2017
Contract Assets		
Prepaid rebates included in Other current assets	$41	$ 52
Prepaid rebates included in Other assets	465	465
Total Contract Assets	$506	$ 517
Contract Liabilities		
Customer discounts and price concessions included in Accrued liabilities	$(1,972)	$ (1,133)
Customer rights of return included in Accrued liabilities	(249)	(462)
Total Contract Liabilities	$(2,221)	$ (1,595)

During the three months period ended March 31, 2018, we recognized revenues of $131 that were included in contract liabilities at the beginning of the period.

The increase in contract liabilities during the three months ended March 31, 2018 is primarily due to net increases in estimated future discounts and price concessions, offset by net settlements of products sold with rights of return.

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Disaggregated Revenue

The following table presents revenues disaggregated by the major markets we serve:

	Three Months Ended March 31, 2018	March 31, 2017
Aero & Defense	$5,103	$4,657
Industrial	20,356	17,112
Medical	9,241	6,814
Telecom & IT	4,525	5,178
Transportation	74,305	66,393
Total	$113,530	$100,154

NOTE 3 – Accounts Receivable

The components of accounts receivable are as follows:

	As of March 31, 2018	December 31, 2017
Accounts receivable, gross	$70,432	$70,941
Less: Allowance for doubtful accounts	(484)	(357)
Accounts receivable, net	$69,948	$70,584

NOTE 4 – Inventories

Inventories consist of the following:

	As of March 31, 2018	December 31, 2017
Finished goods	$10,678	$9,203
Work-in-process	12,089	12,065
Raw materials	21,294	21,150
Less: Inventory reserves	(6,120)	(5,822)
Inventories, net	$37,941	$36,596

NOTE 5 – Property, Plant and Equipment

Property, plant and equipment is comprised of the following:

	As of March 31, 2018	December 31, 2017
Land	$1,137	$1,130
Buildings and improvements	64,457	64,201
Machinery and equipment	229,041	223,650
Less: Accumulated depreciation	(203,950)	(200,734)
Property, plant and equipment, net	$90,685	$88,247

Depreciation expense for the three months ended March 31, 2018	$ 3,763
Depreciation expense for the three months ended March 31, 2017	$ 3,172

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NOTE 6 – Retirement Plans

Pension Plans

Net pension expense (income) for our domestic and foreign plans was as follows:

	Three Months Ended	
	March 31, 2018	March 31, 2017
Net pension expense (income)	$79	$(433)

The components of net pension expense (income) for our domestic and foreign plans include the following:

	Domestic Pension Plans Three Months Ended		Foreign Pension Plans Three Months Ended	
	March 31, 2018	March 31, 2017	March 31, 2018	March 31, 2017
Service cost	$ —	$ —	$ 11	$ 12
Interest cost	1,781	2,068	11	8
Expected return on plan assets (1)	(3,225)	(4,061)	(7)	(5)
Amortization of loss	1,466	1,446	42	38
Other cost due to retirement	—	61	—	—
Expense (income), net	$ 22	$ (486)	$ 57	$ 53

(1) Expected return on plan assets is net of expected investment expenses and certain administrative expenses.

Other Post-retirement Benefit Plan

Net post-retirement expense for our other post-retirement plan includes the following components:

	Three Months Ended	
	March 31, 2018	March 31, 2017
Service cost	$1	$ 1
Interest cost	39	40
Amortization of gain	(12)	(25)
Post-retirement expense	$28	$ 16

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NOTE 7 – Other Intangible Assets

Intangible assets consist of the following components:

	As of March 31, 2018		
	Gross Carrying Amount	Accumulated Amortization	Net Amount
Customer lists/relationships	$64,323	$ (34,536)	$ 29,787
Patents	10,319	(10,319)	—
Technology and other intangibles	44,460	(11,201)	33,259
In process research and development	2,200	—	2,200
Other intangible assets, net	$121,302	$ (56,056)	$ 65,246
Amortization expense for the three months ended March 31, 2018		$ 1,720	

	As of December 31, 2017		
	Gross Carrying Amount	Accumulated Amortization	Net Amount
Customer lists/relationships	$64,323	$ (33,685)	$ 30,638
Patents	10,319	(10,319)	—
Technology and other intangibles	44,460	(10,355)	34,105
In process research and development	2,200	—	2,200
Other intangible assets, net	$121,302	$ (54,359)	$ 66,943
Amortization expense for the three months ended March 31, 2017		$ 1,536	

Remaining amortization expense for other intangible assets as of March 31, 2018 is as follows:

	Amortization expense
2018	$ 5,066
2019	6,754
2020	6,624
2021	6,467
2022	6,230
Thereafter	34,105
Total amortization expense	$ 65,246

NOTE 8 – Costs Associated with Exit and Restructuring Activities

Costs associated with exit and restructuring activities are recorded in the Condensed Consolidated Statement of Earnings as a separate component of Operating earnings.

Total restructuring charges, all related to the June 2016 Plan described below, were as follows:

Three Months Ended

	March 31, 2018	March 31, 2017
Restructuring charges	$1,195	$ 777

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In June 2016, we announced plans to restructure operations by phasing out production at our Elkhart facility by the end of 2018 and transitioning it into a research and development center supporting our global operations ("June 2016 Plan"). Additional organizational changes will also occur in various other locations. During the third quarter of 2017, we revised the June 2016 Plan. The amendment added an additional $1,100 in planned costs related to the relocation of our corporate headquarters in Lisle, IL and our plant in Bolingbrook, IL, both of which will be consolidated into a single facility. The amendment does not impact any additional employees. The total cost of the plan is expected to be approximately $13,400 and will impact approximately 230 employees. The total restructuring liability related to severance and other one-time benefit arrangements under the June 2016 Plan was $1,279 at March 31, 2018, and $1,460 at December 31, 2017. Additional costs related to line movements, equipment charges, and other costs will be expensed as incurred.

The following table displays the planned restructuring charges associated with the June 2016 Plan as well as a summary of the actual costs incurred through March 31, 2018:

June 2016 Plan	Planned Costs	Actual costs incurred through March 31, 2018
Workforce reduction	$3,075	$ 3,089
Building and equipment relocation	9,025	4,548
Other charges	1,300	745
Total restructuring charges	$13,400	$ 8,382

In April 2014, we announced plans to restructure our operations and consolidate our Canadian operations into other existing facilities as part of our overall plan to simplify its business model and rationalize our global footprint (“April 2014 Plan”). These restructuring actions, which were completed during 2015, impacted approximately 120 positions. The remaining restructuring liability related to the April 2014 Plan was $445 at March 31, 2018, and $453 at December 31, 2017.

The following table displays the restructuring liability activity for all plans for the three months ended March 31, 2018:

Combined Plans	
Restructuring liability at January 1, 2018	$1,913
Restructuring charges	1,195
Cost paid	(1,376)
Other activity (1)	(8)
Restructuring liability at March 31, 2018	$1,724

(1) Other activity includes the effects of currency translation and other charges that do not flow through restructuring expense.

NOTE 9 – Accrued Liabilities

The components of accrued liabilities are as follows:

	As of March 31, 2018	December 31, 2017
Accrued product related costs	$5,008	$ 5,297
Accrued income taxes	6,770	5,475
Accrued property and other taxes	2,404	997
Accrued professional fees	2,730	2,228

Contract liabilities	2,221	1,595
Dividends payable	1,321	1,318
Remediation reserves	15,119	17,067
Other accrued liabilities	6,454	7,367
Total accrued liabilities	$42,027	$ 41,344

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NOTE 10 – Contingencies

Certain processes in the manufacture of our current and past products create by-products classified as hazardous waste. We have been notified by the U.S. Environmental Protection Agency, state environmental agencies, and in some cases, groups of potentially responsible parties, that we may be potentially liable for environmental contamination at several sites currently and formerly owned or operated by us. Some sites, such as Asheville, North Carolina and Mountain View, California, are designated National Priorities List sites under the U.S. Environmental Protection Agency's Superfund program. We reserve for probable remediation activities and for claims and proceedings against us with respect to other environmental matters. We record reserves on an undiscounted basis. In the opinion of management, based upon presently available information relating to such matters, adequate provision for probable and estimable costs have been recorded. We do not have any known environmental obligations where a loss is probable or reasonably possible of occurring for which we do not have a reserve, nor do we have any amounts for which we have not reserved because the amount of the loss cannot be reasonably estimated. Due to the inherent nature of environmental obligations, we cannot provide assurance that our ultimate environmental liability will not materially exceed the amount of its current reserve. Our reserve and disclosures will be adjusted accordingly if additional information becomes available in the future.
A roll forward of remediation reserves included in accrued liabilities on the balance sheet is comprised of the following:

	As of March 31, 2018	December 31, 2017
Balance at beginning of period	$17,067	$ 18,176
Remediation expense	85	307
Net remediation payments	(2,033)	(1,416)
Balance at end of the period	$15,119	$ 17,067

Unrelated to the environmental claims described above, certain other claims are pending against us with respect to matters arising in the ordinary conduct of our business. Although the ultimate outcome of any potential litigation resulting from these claims cannot be predicted with certainty, and some may be disposed of unfavorably to us, we believe that adequate provision for anticipated costs have been established based upon all presently available information. Except as noted herein, we do not believe we have any pending loss contingencies that are probable or reasonably possible of having a material impact on our consolidated financial position, results of operations, or cash flows.

NOTE 11 - Debt

Long-term debt was comprised of the following:

	As of March 31, 2018	December 31, 2017
Total credit facility	$300,000	$300,000
Balance outstanding	$74,000	$76,300
Standby letters of credit	$2,065	$2,065
Amount available	$223,935	$221,635
Weighted-average interest rate	2.90 %	2.30 %
Commitment fee percentage per annum	0.25 %	0.25 %

On August 10, 2015, we entered into a new five-year credit agreement (“Revolving Credit Facility”) with a group of banks in order to support our financing needs. The Revolving Credit Facility originally provided for a credit line of $200,000. On May 23, 2016, we requested and received a $100,000 increase in the aggregate revolving credit commitments under the existing credit agreement, which increased the credit line from $200,000 to $300,000.

The Revolving Credit Facility includes a swing line sublimit of $15,000 and a letter of credit sublimit of $10,000. Borrowings under the Revolving Credit Facility bear interest, at our option, at the base rate plus the applicable margin for base rate loans or LIBOR plus the applicable margin for LIBOR loans. We also pay a quarterly commitment fee on the unused portion of the Revolving Credit Facility. The commitment fee ranges from 0.20% to 0.40% based on the our total leverage ratio.

The Revolving Credit Facility requires, among other things, that we comply with a maximum total leverage ratio and a minimum fixed charge coverage ratio. Failure to comply with these covenants could reduce the borrowing availability under the Revolving

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Credit Facility. We were in compliance with all debt covenants at March 31, 2018. The Revolving Credit Facility requires that we deliver quarterly financial statements, annual financial statements, auditor certifications, and compliance certificates within a specified number of days after the end of a quarter and year. Additionally, the Revolving Credit Facility contains restrictions limiting our ability to: dispose of assets; incur certain additional debt; repay other debt or amend subordinated debt instruments; create liens on assets; make investments, loans or advances; make acquisitions or engage in mergers or consolidations; engage in certain transactions with our subsidiaries and affiliates; and make stock repurchases and dividend payments. Interest rates on the Revolving Credit Facility fluctuate based upon the London Interbank Offered Rate and the Company's quarterly total leverage ratio.

We have debt issuance costs related to our long-term debt that are being amortized using the straight-line method over the life of the debt. These costs are included in interest expense in our Condensed Consolidated Statement of Earnings. Amortization expense was approximately $46 for both the three months ended March 31, 2018 and March 31, 2017.

Note 12 - Derivative Financial Instruments

Our earnings and cash flows are subject to fluctuations due to changes in foreign currency exchange rates and interest rates. We selectively use derivative financial instruments including foreign currency forward contracts and interest rate swaps to manage our exposure to these risks.

The use of derivative financial instruments exposes the Company to credit risk, which relates to the risk of nonperformance by a counterparty to the derivative contracts. We manage our credit risk by entering into derivative contracts with only highly rated financial institutions and by using netting agreements.

Foreign Currency Hedges

In January of 2016, we began using forward contracts to mitigate currency risk related to a portion of our forecasted foreign currency revenues and costs. The currency forward contracts are designed as cash flow hedges and are recorded in the Condensed Consolidated Balance Sheets at fair value. At least quarterly, we assess the effectiveness of these hedging relationships based on the total change in their fair value using regression analysis. The effective portion of derivative gains and losses are recorded in accumulated other comprehensive income (loss) until the hedged transaction affects earnings upon settlement, at which time they are reclassified to cost of goods sold or net sales. Ineffectiveness is recorded in other income (expense) in our Condensed Consolidated Statement of Earnings. If it becomes probable that an anticipated transaction that is hedged will not occur by the end of the originally specified time period, we reclassify the gains or losses related to that hedge from accumulated other comprehensive income (loss) to other income (expense).

We continue to monitor the Company's overall currency exposure and may elect to add cash flow hedges in the future. At March 31, 2018, we had a net unrealized gain of $37 in accumulated other comprehensive loss, of which $34 is expected to be reclassified to income within the next 12 months. At March 31, 2017 we had a net unrealized gain of $486 in accumulated other comprehensive income (loss). The notional amount of foreign currency forward contracts outstanding was $25.2 million at March 31, 2018.

Interest Rate Swaps

We use interest rate swaps to convert the revolving credit facility's variable rate of interest into a fixed rate. In the second quarter of 2012, CTS entered into four separate interest rate swap agreements to fix interest rates on $50,000 of long-term debt for the periods January 2013 to January 2017. In the third quarter of 2012, we entered into four additional interest rate swap agreements to fix interest rates on $25,000 of long-term debt for the periods January 2013 to January 2017. In the third quarter of 2016, we entered into three additional interest rate swap agreements to fix interest rates on $50,000 of long-term debt for the periods August 2017 to August 2020. The difference to be paid or received under the terms of the swap agreements will be recognized as an adjustment to interest expense when settled.

These swaps are treated as cash flow hedges and consequently, the changes in fair value were recorded in other comprehensive income (loss). The estimated net amount of the existing gains or losses that are reported in accumulated other comprehensive income (loss) that is expected to be reclassified into earnings within the next twelve months is approximately $424.

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The location and fair values of derivative instruments designated as hedging instruments in the Condensed Consolidated Balance Sheets as of March 31, 2018, are shown in the following table:

	As of March 31, 2018	December 31, 2017
Interest rate swaps reported in Other current assets	$424	$ 278
Interest rate swaps reported in Other assets	$870	$ 693
Foreign currency hedges reported in Other current assets	$34	$ —
Foreign currency hedges reported in Accrued liabilities	$—	$ (742)

The Company has elected to net its foreign currency derivative assets and liabilities in the balance sheet in accordance with ASC 210-20 (Balance Sheet, Offsetting). On a gross basis, there were foreign currency derivative assets of $351 and foreign currency derivative liabilities of $317.

The effect of derivative instruments on the Condensed Consolidated Statements of Earnings is as follows:

	Three Months Ended March 31, 2018	March 31, 2017
Foreign Exchange Contracts:		
Loss recognized in Net sales	$(58)	$(2)
Gain (loss) recognized in Cost of goods sold	108	(144)
Loss recognized in Selling, general and administrative expense	(1)	(3)
Loss recognized in Other income	(1)	(8)
Interest Rate Swaps:		
Benefit recorded in Interest expense	$65	$—
Total gain (loss)	$113	$(157)

NOTE 13 – Accumulated Other Comprehensive (Loss) Income

Shareholders' equity includes certain items classified as accumulated other comprehensive (loss) income ("AOCI") in the Condensed Consolidated Balance Sheets, including:

Unrealized gains (losses) on hedges relate to interest rate swaps to convert the revolving credit facility's variable rate of interest into a fixed rate and foreign currency forward contracts used to hedge our exposure to changes in exchange rates affecting certain revenues and costs denominated in foreign currencies. These hedges are designated as cash flow hedges, and we have deferred income statement recognition of gains and losses until the hedged transactions occur, at which time amounts are reclassified into earnings. Further information related to CTS' derivative financial instruments is included in Note 12 - Derivative Financial Instruments and Note 16 – Fair Value Measurements.

Unrealized gains (losses) on pension obligations are deferred from income statement recognition until the gains or losses are realized. Amounts reclassified to income from AOCI are included in net periodic pension income / (expense). Further information related to our pension obligations is included in Note 6 – Retirement Plans.

Cumulative translation adjustments relate to our non-U.S. subsidiary companies that have designated a functional currency other than the U.S. dollar. We are required to translate the subsidiary functional currency financial statements to dollars using a combination of historical, period-end, and average foreign exchange rates. This combination of rates creates the foreign currency translation adjustment component of other comprehensive (loss) income.

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Changes in exchange rates between the functional currency and the currency in which a transaction is denominated are foreign exchange transaction gains or losses. Transaction gains for the three months ended March 31, 2018 and March 31, 2017 were $1,996 and $395, respectively, which have been included in other income (expense) in the Condensed Consolidated Statement of Earnings.

The components of accumulated other comprehensive (loss) income for the three months ended March 31, 2018, are as follows:

As of December 31, 2017	Gain (Loss) Recognized in OCI	Gain (Loss) Reclassified from AOCI to Income	As of March 31,