

HURCO COMPANIES INC  
Form 10-K  
January 06, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

**FORM 10-K**

(Mark One)

Annual report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the fiscal year ended  
 October 31, 2016 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 No. 0-9143

**HURCO COMPANIES, INC.**

(Exact name of registrant as specified in its charter)

**Indiana**

(State or other jurisdiction of  
incorporation or organization)

**35-1150732**

(I.R.S. Employer Identification Number)

**One Technology Way**

**Indianapolis, Indiana**

(Address of principal executive offices) (Zip code)

**46268**

Registrant's telephone number, including area code

**(317) 293-5309**

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

Securities registered pursuant to Section 12(g) of the Act: **Common Stock, No Par Value**  
(Title of Class)

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). 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, and (2) has been subject to the 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 (§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

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

Indicate by check mark whether the registrant is 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  Non-accelerated filer  Smaller reporting company

(Do not check if a smaller reporting company)

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

The aggregate market value of the registrant's voting stock held by non-affiliates as of April 29, 2016 (the last business day of our most recently completed second quarter) was \$212,837,000.

The number of shares of the registrant's common stock outstanding as of December 12, 2016 was 6,573,103.

DOCUMENTS INCORPORATED BY REFERENCE: Portions of the registrant's Proxy Statement for its 2017 Annual Meeting of Shareholders (Part III).



## **Forward-Looking Statements**

This report contains certain statements that are forward-looking statements within the meaning of federal securities laws. Forward-looking statements can be identified by the fact that they do not relate strictly to historical or current facts. When used in this report, the words “may”, “will”, “should”, “would”, “could”, “anticipate”, “expect”, “plan”, “seek”, “b”, “predict”, “estimate”, “potential”, “project”, “target”, “forecast”, “intend”, “strategy”, “future”, “opportunity”, “assume”, “guid” expressions are intended to identify forward-looking statements. Forward-looking statements are based on current expectations and assumptions that are subject to risks and uncertainties that could cause actual results to differ materially from such forward-looking statements. These risks and uncertainties include, but are not limited to, the risks and other important factors under the heading “Risk Factors” in Part I, Item 1A of this report. You should understand that it is not possible to predict or identify all factors that could cause actual results to differ materially from forward-looking statements. Consequently, you should not consider any list or discussion of such factors to be a complete set of all potential risks or uncertainties. Readers of this report are cautioned not to place undue reliance on these forward-looking statements. While we believe the assumptions on which the forward-looking statements are based are reasonable, there can be no assurance that these forward-looking statements will prove to be accurate. This cautionary statement is applicable to all forward-looking statements contained in this report. We expressly disclaim any obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise. You are advised, however, to consult any further disclosures we make on related subjects in our Form 10-Q, 8-K and 10-K reports and our other filings with the Securities and Exchange Commission (“SEC”).

## **PART I**

### **Item 1. BUSINESS**

#### **General**

Hurco Companies, Inc. is an international, industrial technology company. We design, manufacture and sell computerized (i.e., Computer Numeric Control (“CNC”) machine tools, consisting primarily of vertical machining centers (mills) and turning centers (lathes), to companies in the metal cutting industry through a worldwide sales, service and distribution network. Although the majority of our computer control systems and software products are proprietary, they predominantly use industry standard personal computer components. Our computer control systems and software products are primarily sold as integral components of our computerized machine tool products. We also provide machine tool components, software options, control upgrades, accessories and replacement parts for our products, as well as customer service and training and applications support. As used in this report, the words “we”, “us”, “our”, “Hurco” and the “Company” refer to Hurco Companies, Inc. and its consolidated subsidiaries.

Since our founding in 1968, we have been a leader in the introduction of interactive computer control systems that automate manufacturing processes and improve productivity in the metal parts manufacturing industry. We pioneered

the application of microprocessor technology and conversational programming software for use in machine tools. Our computer control systems can be operated by both skilled and unskilled machine tool operators and yet are capable of instructing a machine to perform complex tasks. The combination of microprocessor technology and patented interactive, conversational programming software in our computer control systems enables operators on the production floor to quickly and easily create a program for machining a particular part from a blueprint or computer aided design file and immediately begin machining that part.

Our executive offices and principal design and engineering operations are headquartered in Indianapolis, Indiana, U.S. Sales, application engineering and service subsidiaries are located in China, France, Germany, India, Italy, Poland, Singapore, South Africa, Taiwan, the United Kingdom, and the U.S. We have manufacturing and assembly operations in Taiwan, the U.S., Italy and China, and distribution facilities in the U.S., the Netherlands, and Taiwan.

During the third quarter of fiscal 2015, we acquired the assets of the machine tool business of Milltronics Manufacturing Company, Inc. and we are operating this U.S. business as a product line through our wholly-owned subsidiary, Milltronics USA, Inc. (“Milltronics”). Milltronics manufactures and sells CNC knee mills, tool room bed mills, vertical machining centers, combination lathes, slant-bed lathes, horizontal machining centers, and bridge mills. During the third quarter of fiscal 2015, we also acquired the assets of the machine tool business of Takumi Machinery Co., Ltd. (“Takumi”), a Taiwanese company that designs and manufactures CNC vertical machining centers, double column machining centers, high speed bridge machines and other machine tools, with sales primarily in Taiwan, China and Europe. Takumi machines are equipped with industrial controls from Fanuc®, Siemens®, Mitsubishi® or Heidenhain® which can be used in high-volume parts manufacturing. We are operating this Taiwanese business as a product line through our wholly-owned subsidiary Hurco Manufacturing Limited (“HML”).

The Milltronics and Takumi product lines contribute to our efforts to expand our consolidated product range, customer base and global platform, and we believe may accelerate emerging market penetration, particularly in strategic markets such as China and South America.

Our strategy is to design, manufacture and sell a comprehensive line of computerized machine tools that help customers in the worldwide metal cutting market increase productivity and profitability. The majority of our machine tools employ proprietary, interactive, computer control technology that increases productivity through ease of operation via interactive conversational and graphical programming software. All of our machine tools deliver high levels of machine performance (speed, accuracy and surface finish quality) that increases productivity. We routinely expand our product offerings to meet customer needs, which has led us to design and manufacture more complex machining centers with advanced capabilities. We bring a disciplined approach to strategically enter new geographic markets, as appropriate.

## **Industry**

Machine tool products are considered capital goods, which makes them part of an industry that has historically been highly cyclical.

Although industry association data for the U.S. machine tool market is available, that market only accounts for approximately 9% of worldwide consumption. Reports available for the U.S. machine tool market include:

- United States Machine Tool Consumption – generated by the Association for Manufacturing Technology, this report includes metal cutting machines of all types and sizes, including segments in which we do not compete
- Purchasing Manager’s Index - developed by the Institute for Supply Management, this report includes activity levels in U.S. manufacturing plants that purchase machine tools
- Capacity Utilization of Manufacturing Companies – issued by the Federal Reserve Board

A limited amount of information is available for foreign markets, and different reporting methodologies are used by various countries. Machine tool consumption data, published by Gardner Publications, Inc., calculates machine tool consumption annually by country. It is important to note that data for foreign countries are based on government reports that may lag 6 to 12 months and, therefore, are unreliable for forecasting purposes.

\*Fanuc® is a registered trademark of GE Fanuc Automation Americas, Inc. Siemens® is a registered trademark of Siemens AG. Mitsubishi® is a registered trademark of Mitsubishi Electric Corporation. Heidenhain® is a registered trademark of HEIDENHAIN CORPORATION, a wholly owned subsidiary of the German company DR. JOHANNES HEIDENHAIN GmbH.

Demand for capital equipment can fluctuate significantly during periods of changing economic conditions. Manufacturers and suppliers of capital goods, such as our company, are often the first to experience these changes in demand. Additionally, since our typical order backlog is approximately 45 days, it is difficult to estimate demand with any reasonable certainty. Therefore, we do not have the benefit of relying on the common leading indicators that other industries use for market analysis and forecasting purposes.

## **Products**

Our core products consist of general purpose computerized machine tools for the metal cutting industry, principally, vertical machining centers (mills) and turning centers (lathes). The majority of our machine tools are equipped and integrated fully with our proprietary software and computer control systems, while the remaining machine tools are equipped with industry standard controls. Additionally, we produce and distribute software options, control upgrades, hardware accessories and replacement parts for our machine tool product lines, and we provide operator training and support services to our customers. We also produce computer control systems and related software for press brake applications that are sold as retrofit units for installation on existing or new press brake machines.

The following table sets forth the contribution of each of our product groups and services to our total revenues during each of the past three fiscal years (in thousands):

### **Net Sales and Service Fees by Product Category**

	Year Ended October 31,					
	2016		2015		2014	
Computerized Machine Tools*	\$195,618	86 %	\$189,712	87 %	\$193,937	87 %
Computer Control Systems and Software †	2,078	1 %	3,085	1 %	3,407	2 %
Service Parts	21,908	10 %	19,375	9 %	17,391	8 %
Service Fees	7,685	3 %	7,211	3 %	7,568	3 %
Total	\$227,289	100%	\$219,383	100%	\$222,303	100%

\* Amounts shown include sales of Milltronics and Takumi computerized machine tools to third parties since the respective dates of those acquisitions.

† Amounts shown do not include computer control systems and software sold as an integrated component of computerized machine systems.

## **Product Portfolio by Brand**

We have three brands of CNC machine tools in our product portfolio: Hurco is the premium brand focused on sophisticated technology. Milltronics is the entry level brand with a simplified control and straightforward feature sets. Takumi is an industry standard brand with machines that are equipped with industry standard controls instead of the proprietary controls found on Hurco and Milltronics machines. Typically, manufacturing facilities that use industry standard controls focus on medium to high production, wherein they run large batches of a few types of parts instead of small batches of many different types of parts. In addition, through our wholly-owned subsidiary LCM Precision Technology S.r.l. ("LCM"), we produce machine tool components and accessories. The main product categories of each brand are outlined below.

The Hurco, Milltronics and Takumi product lines represent a comprehensive product portfolio with more than 150 different models. The combined machine tool product lines also provide benefits related to the development of product enhancements, technologies and models due to leverage of shared resources and cross-utilization of proven engineering designs that allow us to achieve manufacturing cost reductions from economies of scale and manufacturing efficiencies.

### **Hurco CNC Machine Tools**

Hurco computerized machine tools are equipped with a fully integrated interactive computer control system that features our proprietary WinMax<sup>®</sup> software. Our computer control system enables a machine tool operator to create complex two-dimensional or three-dimensional machining programs directly from an engineering drawing or computer-aided design geometry file. An operator with little or no machine tool programming experience can successfully create a program with minimal training and begin machining the part in a short period of time. The control features an operator console with active touch, and incorporates an upgradeable personal computer (PC) platform using a high speed processor with solid rendering graphical programming. In addition, WinMax<sup>®</sup> has a Windows<sup>®</sup> based operating system that enables users to improve shop floor flexibility and software productivity. Companies using computer controlled machine tools are better able to:

- maximize the efficiency of their human resources;
  - make more advanced and complex parts from a wide range of materials using multiple processes;
  - incorporate fast moving changes in technology into their operations to keep their competitive edge; and
- integrate their business into the global supply chain of their customers by supporting small to medium lot sizes for “just in time” initiatives.

Our Windows<sup>®</sup> based control facilitates our ability to meet these customer needs. The familiar Windows<sup>®</sup> operating system coupled with our intuitive conversational style of program creation allows our customers’ operators to create and edit part-making programs without incurring the incremental overhead of specialized computer aided design and computer aided manufacturing programmers. With the ability to transfer most computer aided design data directly into a Hurco program, programming time can be significantly reduced.

Machine tool products today are being designed to meet the demand for machining complex parts with greater part accuracies. Our proprietary controls with WinMax<sup>®</sup> software and high speed processors efficiently handle the large amounts of data these complex part-making programs require, which enable our customers to create parts with higher accuracy at faster speeds. We continue to add technology to our control design as it becomes available. For example, UltiMotion, our patented motion control system, provides significant cycle time reductions and increases the quality of a part’s surface finish. This technology differentiates us in the marketplace and is incorporated into our control.

Our offering of Hurco machining centers, currently equipped with either a dual touch-screen console or a single touch-screen console, consists of the following product lines:

### ***VM Product Line***

The VM product line consists of moderately priced vertical machining centers for the entry-level market.

The design premise of the machining center with a large work cube and a small footprint optimizes the use of available floor space. The VM line consists of five models in four sizes with X-axis (horizontal) travels of 18, 26, 40, and 50 inches.

### ***VMX Product Line***

The VMX product line consists of higher performing vertical machining centers aimed at manufacturers that require greater part accuracy. It is our flagship series of machining centers. The VMX line consists of 12 models in eight sizes with X-axis travels of 24, 26, 30, 42, 50, 60, 64, and 84 inches.

Windows® is a registered trademark of Microsoft Corporation in the United States and other countries.

### ***Five-Axis Product Line***

The five-axis product line is targeted at manufacturers seeking to produce multi-sided parts or true five axis in a single setup. Machines in this product line can yield significant productivity gains for manufacturers that previously had to process each side of a part separately. Additionally, investing in five-axis technology helps our customers to expand their customer base, as they are able to bid on more complex projects that require simultaneous five-axis operations. The five-axis product line consists of 18 models with three different configurations: swivel head, trunnion table, and cantilever.

### ***HS Product Line***

Due to the integral, motorized spindle with a base speed of 18,000 rpm, the HS product line is desirable for the die and mold industry because of that industry's particular interest in the improvement of surface finish quality and the reduction of cycle time. Additionally, this product line offers us the opportunity to expand our customer base to manufacturers that produce larger batches. The HS product line consists of four models with X-axis travels of 24, 30, 42, and 60 inches.

### ***HMX Product Line***

The HMX product line is beneficial to manufacturers entering production manufacturing versus small batch manufacturing. The HMX machines have expanded tool capacity, a comprehensive chip management system, a built-in pallet changer, and a box-in-box design supported at both the top and bottom to increase rigidity for long production runs and heavy cuts. The HMX product line consists of three models in three sizes with X-axis travels of 24, 32, and 41 inches.

### ***HBMX Product Line***

The HBMX product line is beneficial to manufacturers that build custom machinery and parts for a multitude of industries, such as packaging, pharmaceutical, automotive, energy, and medical. Additionally, boring mills are also used to repair and/or rebuild large components. The HBMX boring mill product line consists of four models with X-axis travels of 55, 79, 94, and 120 inches.

***TM/TMM Product Line***

The TM/TMM product line of slant-bed lathes (horizontal turning centers) is designed for entry-level job shops and contract manufacturers seeking efficient processing of small to medium lot sizes. There is one TM model in seven sizes, measured by chuck size: the TM6, TM8, TM10, TM12, TM18, TM18L, and TM18BB. The TM18BB big bore turning center targets the energy and aerospace industries because it has a larger chuck diameter and bigger bar capacity for larger parts. We added motorized tooling on the lathe turret to further enhance the capability of the TM turning centers and designated it as the TMM product line. These turning centers with live tooling allow our customers to complete a number of secondary milling, drilling and tapping operations while the part is still held in the chuck after the turning operations are complete, which provides significant productivity gains. The TMM product line consists of three models: TMM8, TMM10, and TMM12.

***TMX Product Line***

The TMX product line consists of high performance turning centers. There are six models in two sizes. The TMXMY models are equipped with an additional axis and motorized live tooling while the TMXMYS models also have an additional spindle.

***DCX Product Line***

The double column DCX series includes five models in three sizes. These 2-meter, 3-meter, and 4-meter machining centers are designed to facilitate production of large parts and molds often required by the aerospace, energy and custom machinery industries.

### ***New Product Lines***

We introduced the HTM30, an open-bed mill that is beneficial for tool room applications. The BX40 is a bridge mill designed for heavy cuts with a high-speed 18K spindle utilizing the frame design of the bridge mill with a trunnion table for 5-axis machining. The HM1700i and HM1700Ri are both horizontal mills that are equipped with a spindle that is ideal for both high and low end torque operations; however, the HM1700Ri has an embedded rotary torque table to facilitate increased production efficiencies. Additionally, we introduced a 3D print head technology that allows a Hurco CNC machine to be used for 3D printing, which is advantageous for prototyping.

### **Milltronics CNC Machine Tools**

Our Milltronics line of CNC machine tools is designed for excellent value with more standard features for the price versus market leaders. We manufacture and sell these machine tools with fully integrated interactive computer control systems that are also compatible with G & M Code programs (generated from CAD/CAM software) and conversational visual aid programming. These straightforward and easy-to-use control systems are available in two versions, the Series 8200-B for tool room products and the more advanced Series 9000 offered on our new vertical machining centers and bridge mills.

The Milltronics portfolio consists of the following product lines:

#### ***VM General Purpose (GP) Product Line***

The VM-GP product line consists of attractively-priced vertical machining centers designed for job shops, prototype, R & D and other general machining applications. These belt-driven models are 40-taper and available in four different sizes – all with the Series 9000 control. Customers can choose models with X-axis (horizontal) travels of 25, 30, 40 or 50 inches.

#### ***VM Inline Performance (IL) Product Line***

The VM-IL product line consists of moderately-priced performance vertical machining centers for high-speed applications such as tool, die and mold, aerospace or medical machining. Featuring heavier castings, faster motion and

inline spindles, these 40-taper machines include the Series 9000 control and are available in four sizes. Models include X-axis travels of 30, 42, 50 or 60 inches.

***VM Extra Power (XP) Product Line***

The VM-XP product line consists of moderately-priced vertical machining centers for more demanding metal removal applications such as castings or forgings. These 50-taper models are either gear driven or heavy-duty belt driven and include the Series 9000 control. Customers can choose from three different models with X-axis travels of 43, 50 or 60 inches.

***BR Product Line***

The BR product line consists of high-speed bridge mills that are used in pattern shops and the aerospace industry in addition to job shops, due to the large table and travels that support a wide range of part sizes. BR machines have inline spindles and are available as six models in three sizes with X-axis travels of 100, 150, and 200 inches. BR machines offer the Series 9000 control.

### ***MM/MB/RH Product Line***

Products with the MM/MB or RH designation are part of the tool room bed mill category, which are machines that do not have an enclosure, also referred to as open bed machines. Typical applications include general machining, job shops, prototype or maintenance and repair. Available with quill head or rigid head designs, there are six models in four sizes with X-axis travels of 30, 40, 60 and 78 inches. These easy-to-use machines feature the Series 8200-B control.

### ***SL Product Line***

The SL product line of slant-bed lathes (horizontal turning centers) is designed for entry-level job shops and contract manufacturers seeking efficient processing of small to medium lot sizes. There are three models with chuck sizes of 6, 10, and 12 inches. These compact machines feature the Series 8200-B control.

### ***ML Product Line***

The ML product line consists of combination lathes that the customer can configure for either tool room or production applications with the option to add live tooling. There are 17 models available in a variety of thru hole sizes and in the following six swing-over bed diameters: 17, 19, 23, 27, 36, and 39.7 inches. These flexible machines feature the Series 8200-B control.

### ***Takumi CNC Machine Tools***

Our Takumi machine tools feature industry standard CNC controls, including Fanuc®, Siemens®, Mitsubishi® or Heidenhain®. Models include drill and tap machines; three-axis vertical machining centers with linear guides; three-axis vertical machining centers with box ways; high-speed, double column vertical machining centers; and heavy duty, double column machining centers. With the addition of the Takumi brand, we have expanded our customer base to include manufacturers who opt for industrial controls. Generally, manufacturers who use industrial controls have production-oriented operations where they run medium to large batches of just a few different types of parts.

The Takumi portfolio consists of the following product lines:

***VT Series***

The VT Series includes one high-speed drill and tap machine. Model VT500 features fast tool change times and rapid spindle acceleration/deceleration. This three-axis machine is designed for high volume production applications such as automotive parts or electronics components.

***VC Series***

The VC Series vertical machining centers are fast, three-axis linear guide machining centers designed for customers doing batch or production work. The VC machines are available in two sizes with X-axis travels of 34 and 42 inches.

***V Series***

The V Series vertical machining centers are heavy duty, box way machines built for tough applications such as roughing cast iron. These three-axis, massive machines feature belt or geared spindles to provide maximum torque. The V Series product line includes eight models with X-axis travels of 39, 43, 47, 60, 70, 78, 86, and 126 inches.

***H Series***

Designed to produce parts that require high precision and superior surface finishes, H Series machines offer an extremely rigid and thermally stable double column design. These three-axis models feature high-speed direct drive or built-in HSK spindles with up to 20,000 rpm, and offer a 24,000 rpm spindle and 36,000 rpm spindle as options. The H Series product line consists of eight models in seven different sizes with X-axis travels of 30, 35, 40, 53, 63, 86, and 126 inches.

### ***G Series***

Designed specifically for the machining of graphite or copper electrodes used in electrical discharge machining (EDM), G Series machines offer the same extremely rigid and thermally stable double column design of the H Series, featuring high-speed direct drive or built-in HSK spindles with up to 20,000 rpm. The G Series product line consists of two models with X-axis travels of 30 and 40 inches.

### ***BC Series***

The BC Series machine is a double column three-axis machining center designed for heavy cutting and applications that require high power and torque, such as mold and die. This model includes a 6,000 rpm geared-head design with X-axis travels of 82 inches.

### ***Other Control Systems and Software***

The following machine tool computer control systems and software products are sold directly to end-users and/or to original equipment manufacturers.

#### ***Autobend®***

Autobend® computer control systems are applied to metal bending press brake machines that form parts from sheet metal and steel plate. They consist of a microprocessor-based computer control and back gauge (an automated gauging system that determines where the bend will be made). We have manufactured and sold the Autobend® product line since 1968. We currently market two models of our Autobend® computer control systems for press brake machines, in combination with six different back gauges as retrofit units for installation on existing or new press brake machines.

#### ***Software Products***

In addition to our standard computer control features, we offer software option products for part programming. These products are sold to users of our Hurco computerized machine tools equipped with our dual touch-screen or single touch-screen consoles featuring WinMax® control software. Each international division packages the options as appropriate for its market. The most common options include: Advanced Verification Graphics, Swept Surface, DXF Transfer, UltiMonitor, UltiPocket with Helical Ramp Entry and Insert Pockets, Conversational Part and Tool Probing, Tool and Material Library, NC/Conversational Merge, Job List, Stream Load, Linear Thermal Compensation, Thread Repair, and Simultaneous Five-Axis Contouring.

The Advanced Verification Graphics option displays a picture of the rendered part on the screen of the control that can be viewed from any angle. The detail allows the customer to evaluate how the part is programmed to be machined before cutting commences, which eliminates the need to scrap expensive material.

Our Swept Surface software option simplifies programming of 3D contours and significantly reduces programming time.

The DXF Transfer software option increases operator productivity because it eliminates manual data entry of part features by transferring AutoCAD®\* drawing files directly into our computer control or into our desktop programming software, WinMax® Desktop.

UltiMonitor is a web-based productivity, management and service tool that enables customers to monitor, inspect and receive notifications about their Hurco machines from any location where they can access the internet. Customers can transfer part designs, receive event notifications via email or text, access diagnostic data, monitor the machine via webcam and communicate with the machine operator.

\* AutoCAD® is a registered trademark of Autodesk, Inc., and/or its subsidiaries/ affiliates in the U.S. and/or other countries.

UltiPocket with Helical Ramp Entry and Insert Pockets automatically calculates the tool path around islands, eliminating the arduous task of plotting these shapes. Islands can also be rotated, scaled and repeated.

Conversational Part and Tool Probing options permit the computerized dimensional measurement of machined parts and the associated cutting tools. This “on-machine” technique improves the throughput of the measurement process when compared to traditional “off-machine” approaches.

The Tool and Material Library option stores the tool and material information with the machine instead of storing it with each individual part program. The user enters the tool data and geometry one time and chooses the particular tool from the list when it is needed. Additionally, the library reads the part program and automatically locates the tool or displays an alert if the tool does not exist. In addition to saving time, the Tool and Material Library eliminates the need to enter information repeatedly, and can prevent common tool crash conditions.

NC/Conversational Merge lets the user incorporate conversational features, such as tool probing, pattern operations, and scaling into existing G-Code programs.

Job List provides an intuitive way to group files together and run them sequentially without operator intervention, which promotes automation, lights-out machining, program stitching, file bundling, and adaptive processes.

Stream Load allows the user to run very large NC files without the need to upload the entire file into the control’s memory to avoid exceeding memory limits.

Linear Thermal Compensation is a feature that allows the user to specify corrections to compensate for the effects of thermal growth in high speed machining applications.

Thread Repair is a feature for turning applications that provides an efficient way to repair existing threads, which is especially beneficial for large pipes and other parts manufactured for the oil/energy sector.

Simultaneous Five-Axis Contouring software enables a five-axis machine to command motion concurrently on all axes. This allows the user to create continuous tool-paths along complex geometries with only a single machine/part setup, providing increased productivity along with the performance benefits of using shorter cutting tools. The sale of

simultaneous five-axis contouring software is subject to government export licensing requirements.

**LCM Machine Tool Components and Accessories**

Based in Italy, LCM designs, manufactures and sells mechanical and electro-mechanical components and accessories for machine tools. LCM's direct drive spindle, swivel head, and rotary torque table are used in our SRT line of five-axis machining centers to achieve simultaneous five-axis machining.

***CNC Rotary Tables***

LCM has five lines of CNC rotary tables for both horizontal and vertical-horizontal positioning. Customers can choose rotary tables with either hydraulic or pneumatic clamping systems. Additionally, LCM offers CNC rotary tables powered by either a torque motor or a high-precision mechanical transmission.

***CNC Tilt Tables***

LCM has seven lines of CNC tilting rotary tables, of which four lines are intended specifically for five-axis machining centers. Each of the seven lines is differentiated by the technology used for clamping (hydraulic or pneumatic) and by the type of transmission (either mechanical transmission or torque motor).

### *Swivel Heads and Electro-spindles*

LCM has two primary lines of swivel heads that enable the spindle axis to be tilted with continuous motion and one line of electro-spindles (built-in motors for swivel heads). The two lines of swivel heads are differentiated by the type of transmission (either mechanical transmission or torque motor).

### **Parts and Service**

Our service organization provides installation, warranty, operator training and customer support for our products on a worldwide basis. In the United States, our principal distributors have the primary responsibility for machine installation and warranty service and support for product sales. Our service organization also sells software options, computer control upgrades, accessories and replacement parts for our products. Our after-sales parts and service business strengthens our customer relationships and provides continuous information concerning the evolving requirements of end-users.

### **Manufacturing**

Our computerized metal cutting machine tools are manufactured and assembled to our specifications primarily by our wholly-owned subsidiaries in Taiwan (HML) and Waconia, Minnesota (Milltronics). HML and Milltronics conduct final assembly operations and are supported by a network of contract suppliers of components and sub-assemblies that manufacture components for our products. Our facility in Ningbo, China, focuses on the machining of castings to support HML's production in Taiwan. The LCM line of electro-mechanical components and accessories for machine tools is designed and manufactured in Italy. Our facility in Indianapolis, Indiana, also conducts final assembly operations for certain Hurco VMX machines for the American market and manufactures certain electro-spindle components for LCM.

We have a contract manufacturing agreement for computer control systems with Hurco Automation, Ltd. ("HAL"), a Taiwanese company in which we have a 35% ownership interest. This company produces all of our computer control systems to our specifications, sources industry standard computer components and our proprietary parts, performs final assembly and conducts test operations.

We work closely with our subsidiaries, key component suppliers and HAL to ensure that their production capacity will be sufficient to meet the projected demand for our machine tool products. Many of the key components used in

our machines can be sourced from multiple suppliers. However, any prolonged interruption of operations or significant reduction in the capacity or performance capability at any of our manufacturing facilities, or at any of our key component suppliers, could have a material adverse effect on our operations.

### **Marketing and Distribution**

We principally sell our products through more than 195 independent agents and distributors throughout North and South America (the Americas), Europe and Asia. Although some distributors carry competitive products, we are the primary line for the majority of our distributors globally. We also have our own direct sales and service organizations in China, France, Germany, India, Italy, Poland, Singapore, South Africa, Taiwan, the United Kingdom and certain parts of the United States, which are among the world's principal machine tool consuming markets.

Approximately 91% of the worldwide demand for computerized machine tools and computer control systems is outside of the U.S. In fiscal 2016, approximately 69% of our revenues were derived from customers outside of the U.S. No single end-user or distributor of our products accounted for more than 5% of our total sales and service fees. The end-users of our products are precision tool, die and mold manufacturers, independent job shops, specialized short-run production applications within large manufacturing operations and manufacturing facilities that focus on medium to high run production wherein they run large batches of a few types of parts instead of small batches of many different parts. Industries served include aerospace, defense, medical equipment, energy, automotive/ transportation, electronics and computer industries.

We also sell our Autobend® computer control systems to original equipment manufacturers of new metal fabrication machine tools that integrate them with their own products prior to the sale of those products to their own customers, to retrofitters of used metal fabrication machine tools that integrate them with those machines as part of the retrofitting operation, and to end-users that have an installed base of metal fabrication machine tools, either with or without related computer control systems.

### **Demand**

We believe demand for our products is driven by advances in industrial technology and the related demand for automated process improvements. Other factors affecting demand include:

- the need to continuously improve productivity and shorten cycle time;
- an aging machine tool installed base which will require replacement with more advanced technology;
- the industrial development of emerging markets in Latin America, Asia and Eastern Europe; and
  - the declining supply of skilled machinists.

Demand for our products is also highly dependent upon economic conditions and the general level of business confidence, as well as such factors as production capacity utilization and changes in governmental policies regarding tariffs, corporate taxation, fluctuations in foreign currencies, and other investment incentives.

### **Competition**

We compete with many other machine tool producers in the United States and foreign countries. Most of our competitors are larger and have greater financial resources than our company. Major worldwide competitors include

DMG Mori Seiki Co., Ltd., Mazak, Haas Automation, Inc., Hardinge Inc., Doosan, Okuma Machinery Works Ltd, Hyundai and Feeler.

Through our subsidiary LCM, we compete with manufacturers of machine tool components and accessories such as IBAG, Kessler, Peron Speed, GSA Technology Co., LTD and Duplomatic Automation.

We strive to compete by developing patentable software and other proprietary features that offer enhanced productivity, technological capabilities and ease of use. We offer our products in a range of prices and capabilities to target a broad potential market. We also believe that our competitiveness is aided by our reputation for reliability and quality, our strong international sales and distribution organization, and our extensive customer service organization.

### **Intellectual Property**

We consider the majority of our products to be proprietary. Various features of our Hurco and Milltronics control systems and machine tools employ technologies covered by patents and trademarks that are material to our business. We also own additional patents covering new technologies that we have acquired or developed, and that we are planning to incorporate into our control systems in the future.

## **Research and Development**

In the fiscal years set forth below, we incurred both (i) non-capitalized research and development expenditures for new products, significant product improvements and (ii) capitalized expenditures related to software development projects as follows (in thousands):

Fiscal Year	Non-Capitalized Research and Development	Capitalized Software Development
2016	\$ 4,900	\$ 2,200
2015	\$ 3,900	\$ 1,400
2014	\$ 3,400	\$ 1,000

## **Employees**

We had approximately 758 full-time employees at the end of fiscal 2016, none of whom are covered by a collective-bargaining agreement or represented by a union. We have experienced no employee-generated work stoppages or disruptions, and we consider our employee relations to be satisfactory.

## **Geographic Areas**

Financial information concerning the geographic areas in which we sell our products is set forth in Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations and in Note 15 of Notes to Consolidated Financial Statements. Some of the risks of doing business on a global basis are described in Item 1A. Risk Factors below.

## **Backlog**

For information on orders and backlog, see Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

**Availability of Reports and Other Information**

Our website can be found at [www.hurco.com](http://www.hurco.com). We use this website as a means of disclosing pertinent information about the company, free of charge, including:

Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q, proxy materials, Current Reports on Form 8-K and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), as soon as reasonably practicable after we electronically file that material with or furnish it to the SEC;

press releases on quarterly earnings, product announcements, legal developments and other material news that we may post from time to time;

corporate governance information including our Corporate Governance Principles, Code of Business Conduct and Ethics, information concerning our Board of Directors and its committees, including the charters of the Audit Committee, Compensation Committee, Nominating and Governance Committee and other governance-related policies; and

- opportunities to sign up for email alerts and RSS feeds to have information provided in real time.

The information available on our website is not incorporated by reference in, or a part of, this or any other report we file with, or furnish to, the SEC.

**Item 1A. RISK FACTORS**

In this section we describe what we believe to be the material risks related to our business. The risks and uncertainties described below or elsewhere in this report are not the only ones to which we are exposed. Additional risks and uncertainties not presently known and/or risks we currently deem immaterial may also adversely affect our business and operations. If any of the developments included in the following risks were to occur, our business, financial condition, results of operations, cash flows or prospects could be materially adversely affected.

*The cyclical nature of our business causes fluctuations in our operating results.*

The machine tool industry is highly cyclical and changes in demand can occur abruptly in the geographic markets we serve. As a result of this cyclical nature, we have experienced significant fluctuations in our sales, which, in periods of reduced demand, have adversely affected our results of operations and financial condition.

*Uncertain global economic conditions, may adversely affect overall demand.*

We typically sell the majority of our larger high-performance VMX machines in Europe, which makes us particularly sensitive to economic and market conditions in that region. Economic uncertainty and business downturns in the U.S., European and Asian Pacific markets adversely affect our results of operations and financial condition.

*Our international operations pose additional risks that may adversely impact sales and earnings.*

During fiscal 2016, approximately 69% of our revenues were derived from sales to customers located outside of the U.S. In addition, our main manufacturing facilities are located outside of the U.S. Our international operations are subject to a number of risks, including:

- trade barriers;
- regional economic uncertainty;
- differing labor regulation;
- governmental expropriation;
- domestic and foreign customs and tariffs;

current and changing regulatory environments affecting the importation and exportation of products and raw materials;

- difficulty in obtaining distribution support;
- difficulty in staffing and managing widespread operations;
- differences in the availability and terms of financing;
- political instability and unrest;
- changes in tax regulations and rates in foreign countries; and

changes in the European Union and Asia may adversely affect business activity and economic conditions globally and could continue to contribute to instability in global financial and foreign exchange markets, as well as disrupting the free movement of goods, services and people between countries.

Quotas, tariffs, taxes or other trade barriers could require us to change manufacturing sources, reduce prices, increase spending on marketing or product development, withdraw from or not enter certain markets or otherwise take actions that could be adverse to us. Also, in some foreign jurisdictions, we may be subject to laws limiting the right and ability of entities organized or operating therein to pay dividends or remit earnings to affiliated companies unless specified conditions are met. These factors may adversely affect our future operating results. The vast majority of our products are shipped from our manufacturing facility in Taiwan from the Port of Taichung to four ports of destination: Los Angeles, California, Tacoma, Washington, Venlo, the Netherlands, and Shanghai, China. Changes in customs requirements, as a result of national security or other constraints put upon these ports, may also have an adverse impact on our results of operations.

Additionally, we must comply with complex foreign and U.S. laws and regulations, such as the U.S. Foreign Corrupt Practices Act, the U.K. Bribery Act, and other foreign laws prohibiting corrupt payments to governmental officials, and anti-competition regulations. Violations of these laws and regulations could result in fines and penalties, criminal sanctions, restrictions on our business conduct and on our ability to offer our products in one or more countries, and could also materially affect our brand, our ability to attract and retain employees, our international operations, our business and our operating results. Although we have implemented policies and procedures designed to ensure compliance with these laws and regulations, there can be no assurance that our employees, contractors, or agents in foreign countries will not violate our policies.

***We depend on limited sources for our products.***

We depend on our wholly-owned subsidiaries, Hurco Manufacturing Limited, Ningbo Hurco Manufacturing Limited, Milltronics USA, Inc., and LCM Precision Technology S.r.l., to produce our machine tools and electro-mechanical components and accessories in Taiwan, China, the U.S. and Italy, respectively. We also depend on our 35% owned affiliate, HAL, and other key third party suppliers to produce our computer control systems and key components, such as motors and drives for our machine tools. An unplanned interruption in manufacturing would have a material adverse effect on our results of operations and financial condition. Such an interruption could result from a change in the political environment or a natural disaster, such as an earthquake, typhoon, or tsunami. Also, any interruption in service by one of our key component suppliers, if prolonged, could have a material adverse effect on our results of operations and financial condition.

***Fluctuations in the exchange rates between the U.S. Dollar and any of several foreign currencies can increase our costs and decrease our revenues.***

Our sales to customers located outside of the U.S., which generated approximately 69% of our revenues in fiscal 2016, are invoiced and received in several foreign currencies, primarily the Euro, Pound Sterling and Chinese Yuan. Therefore, our results of operations and financial condition are affected by fluctuations in exchange rates between these currencies and the U.S. Dollar, both for purposes of actual conversion and for financial reporting purposes. In addition, we are exposed to exchange risk associated with our purchases of materials and components for our Taiwan manufacturing operations, which are primarily made in the New Taiwan Dollar and the Euro. We hedge our foreign currency exposure with the purchase of forward exchange contracts. These hedge contracts only mitigate the impact of changes in foreign currency rates that occur during the term of the related contract period and carry risks of counter-party failure. There can be no assurance that our hedges will have their intended effects.

***Our competitive position and prospects for growth may be diminished if we are unable to develop and introduce new and enhanced products on a timely basis that are accepted in the market.***

The machine tool industry is subject to technological change, evolving industry standards, changing customer requirements, and improvements in and expansion of product offerings. Our ability to anticipate changes in technology, industry standards, customers' requirements and competitors' product offerings and to develop and introduce new and enhanced products on a timely basis that are accepted in the market, are significant factors in maintaining and improving our competitive position and growth prospects. If the technologies or standards used in our products become obsolete or fail to gain widespread commercial acceptance, our business would be materially adversely affected. Although we believe that we have the technological capabilities to remain competitive, developments by others may render our products or technologies obsolete or noncompetitive.

***We compete with larger companies that have greater financial resources, and our business could be harmed by competitors' actions.***

The markets in which our products are sold are extremely competitive and highly fragmented. In marketing our products, we compete with other manufacturers in terms of quality, reliability, price, value, delivery time, service and technological characteristics. We compete with a number of U.S., European and Asian competitors, most of which are larger, have substantially greater financial resources and have been supported by governmental or financial institution subsidies and, therefore, may have competitive advantages over us. While we believe our product lines compete effectively, our financial resources are limited compared to those of most of our competitors, making it challenging to remain competitive.

***Fluctuations in the price of raw materials, especially steel and iron, could adversely affect our sales, costs and profitability.***

We manufacture products with a high iron and steel content. The availability and price for these and other raw materials are subject to volatility due to worldwide supply and demand forces, speculative actions, inventory levels, exchange rates, production costs and anticipated or perceived shortages. In some cases, those cost increases can be passed on to customers in the form of price increases; in other cases they cannot. If the prices of raw materials increase and we are not able to charge our customers higher prices to compensate, our results of operations would be adversely affected.

***Regulations related to "conflict minerals" may cause us to incur additional expenses and could limit the supply and increase the cost of certain metals used in manufacturing our products.***

The SEC requires disclosure by public companies of specified minerals, known as conflict minerals, that are necessary to the functionality or production of products manufactured or contracted to be manufactured. The rule requires a disclosure report to be filed annually with the SEC, and requires companies to perform due diligence, disclose and report whether or not such minerals originate from the Democratic Republic of Congo or an adjoining country. The rule could affect sourcing at competitive prices and availability in sufficient quantities of certain minerals used in the manufacture of components that are incorporated into our products, including tin, tantalum, gold and tungsten. The number of suppliers that provide conflict-free minerals may be limited. In addition, there may be material costs associated with complying with the disclosure requirements, such as costs related to the due diligence process of determining the source of certain minerals used in our products, as well as costs of possible changes to products, processes, or sources of supply as a consequence of such verification activities. We may not be able to sufficiently verify the origins of the relevant minerals used in components manufactured by third parties through our due diligence procedures, which may harm our reputation. We may also encounter challenges to satisfy those customers that require that all of the components of our products be certified as conflict-free, which could place us at a competitive

disadvantage if we are unable to do so.

*Due to future changes in technology, changes in market demand, or changes in market expectations, portions of our inventory may become obsolete or excessive.*

The technology within our products evolves, and we periodically bring new versions of our machines to market. The phasing out of an old product involves estimating the amount of inventory required to satisfy the final demand for those machines and to satisfy future repair part needs. Based on changing customer demand and expectations of delivery times for repair parts, we may find that we have either obsolete or excess inventory on hand. Because of unforeseen future changes in technology, market demand or competition, we might have to write off unusable inventory, which would adversely affect our results of operations.

*Acquisitions could disrupt our operations and harm our operating results.*

In July 2015, we acquired a CNC machine tool business in Minnesota, U.S. (Milltronics) and a CNC machine tool business in Taiwan (Takumi). We may seek additional opportunities to expand our product offerings or the markets we serve by acquiring other companies, product lines, technologies and personnel. Acquisitions involve numerous risks, including the following:

- difficulties integrating the operations, technologies, products, and personnel of an acquired company;
    - diversion of management's attention from normal daily operations of the business;
  - potential difficulties completing projects associated with in-process research and development;
  - difficulties entering markets in which we have no or limited prior experience, especially when competitors in such markets have stronger market positions;
    - initial dependence on unfamiliar supply chains or relatively small supply partners;
    - insufficient revenues to offset increased expenses associated with acquisitions;
    - the potential loss of key employees of the acquired companies; and
- potential for recording goodwill and intangible assets that later can be subject to impairment.

Acquisitions may also cause us to:

- issue common stock that would dilute our current shareholders' percentage ownership;
  - assume liabilities of an acquired company;
- record goodwill and non-amortizable intangible assets that will be subject to impairment testing on a regular basis and potential periodic impairment charges;
  - incur amortization expenses related to certain intangible assets;
- incur large acquisition and integration costs, immediate write-offs, and restructuring and other related expenses; and
  - become subject to litigation.

Mergers and acquisitions are inherently risky. No assurance can be given that our acquisitions will be successful. Further, no assurance can be given that an acquisition will not adversely affect our business, operating results, or financial condition. Failure to manage and successfully integrate an acquisition could harm our business and operating results in a material way. Even when an acquired company has already developed and marketed products, there can be no assurance that enhancements to those products will be made in a timely manner or that pre-acquisition due diligence will identify all possible issues that might arise with respect to such products.

Risks related to new product development also apply to acquisitions. For additional information, please see the risk factor above entitled, "Due to future changes in technology, changes in market demand, or changes in market expectations, portions of our inventory may become obsolete or excessive."

***Assets may become impaired, requiring us to record a significant charge to earnings.***

We review our assets, including intangible assets such as goodwill, for indications of impairment when events or changes in circumstances indicate the carrying value may not be recoverable. We could be required to record a significant charge to earnings in our financial statements for the period in which any impairment of these assets is determined, which would adversely affect our results of operations for that period.

*We may experience negative or unforeseen tax consequences.*

We may experience negative or unforeseen tax consequences. We review the probability of the realization of our net deferred tax assets each period based on forecasts of taxable income in both the U.S. and foreign jurisdictions. This review uses historical results, projected future operating results based upon approved business plans, eligible carryforward periods, tax-planning opportunities and other relevant considerations. Adverse changes in the profitability and financial outlook in the U.S. or foreign jurisdictions may require the creation of a valuation allowance to reduce our net deferred tax assets. Such changes could result in material non-cash expenses in the period in which the changes are made and could have a material adverse impact on our results of operations and financial condition. We also earn a significant amount of our operating income from outside the U.S., and any repatriation of funds representing earnings of foreign subsidiaries may significantly impact our effective tax rates. In addition, there have been proposals to change U.S. tax laws that would significantly impact how U.S. multinational corporations are taxed on domestic and foreign earnings. Although we cannot predict whether or in what form this proposed legislation will pass, if enacted it could have a material benefit or adverse impact on our tax expense and cash flow.

***Our continued success depends on our ability to protect our intellectual property.***

Our future success depends in part upon our ability to protect our intellectual property. We rely principally on nondisclosure agreements, other contractual arrangements, trade secret law, trademark registration and patents to protect our intellectual property. However, these measures may be inadequate to protect our intellectual property from infringement by others or prevent misappropriation of our proprietary rights. In addition, the laws of some foreign countries do not protect proprietary rights to the same extent as do U.S. laws. Our inability to protect our proprietary information and enforce our intellectual property rights through infringement proceedings could have a material adverse effect on our business, financial condition and results of operations.

***The unanticipated loss of current members of our senior management team and other key personnel may adversely affect our operating results.***

The unexpected loss of members of our senior management team or other key personnel could impair our ability to carry out our business plan. We believe that our future success will depend in part on our ability to attract and retain highly skilled and qualified personnel. The loss of senior management or other key personnel may adversely affect our operating results as we incur costs to replace the departed personnel and potentially lose opportunities in the transition of important job functions.

***If our network and system security measures are breached and unauthorized access is obtained to our data, to our customers' or vendors' data, or to our critical information technology systems, we may incur legal and financial exposure and liabilities.***

As part of our business, we store our data and certain data about our customers and vendors in our information technology systems. If a third party gained unauthorized access to our data, including any data regarding our customers or vendors, the security breach could expose us to risks, including loss of business, litigation and possible liability. Our security measures may be breached as a result of third-party action, including intentional misconduct by computer hackers, employee error, malfeasance or otherwise. Additionally, third parties may attempt to fraudulently induce employees or customers into disclosing sensitive information such as user names, passwords or other information to gain access to our customers' data or our data, including our intellectual property and other confidential business information, or our information technology systems. Although we work closely with industry recognized manufacturers supporting the security measures we have employed in an effort to keep our technology current with the ongoing threats, the techniques used to obtain unauthorized access, or to sabotage systems, change frequently, and therefore we may be unable to anticipate these techniques or to implement adequate preventative measures. Any security breach could result in: the unauthorized publication of our confidential business or proprietary information; the unauthorized release of customer or vendor data and payment information; a loss of confidence by our customers; damage to our reputation; a disruption to our business; litigation and legal liability; and a negative impact on our

future sales. In addition, the cost and operational consequences of implementing further data protection measures could be significant.

**Item 1B. Unresolved Staff Comments**

None.

**Item 2. PROPERTIES**

The following table sets forth the principal use, location, and size of each of our facilities:

<b>Principal Uses</b>	<b>Locations</b>	<b>Square Footage</b>
Corporate headquarters, design and engineering, product testing, sales and marketing, application engineering, customer service, manufacturing and assembly	Indianapolis, Indiana, U.S. (1)	165,000
	Taichung, Taiwan	407,500
Manufacturing, assembly, sales, application engineering and customer service	Waconia, Minnesota, U.S.	97,700
	Castell'Alfero, Italy	32,300
Manufacturing	Ningbo, China	31,000
	High Wycombe, England	16,000
Sales, application engineering and customer service	Benoni, South Africa	3,200
	Paris, France	9,700
	Munich and Verl, Germany	20,100
	Milan, Italy	13,800
	Venlo, the Netherlands	9,700
	Toh Guan, Singapore	3,900
	Shanghai, Dongguan, Shenyang, Kunshan and Beijing, China	2,800
	Chennai, Delhi, Coimbatore, and Pune India	13,900
	Liegnitz, Poland	2,900
	Grand Rapids, Michigan, U.S.	3,700
	Ball Ground, Georgia, U.S.	5,200

(1) Approximately 9,400 square feet is leased to third-parties under leases that will expire February 28, 2017, April 30, 2017 and April 30, 2018.

We own the Indianapolis facility and lease all other facilities. The leases have terms expiring at various dates ranging from January 2017 to March 2024. We believe that all of our facilities are well maintained and are adequate for our needs now and in the foreseeable future. We do not believe that we would experience any difficulty in replacing any of the present facilities if any of our leases were not renewed at expiration.

**Item 3. LEGAL PROCEEDINGS**

We are involved in various claims and lawsuits arising in the normal course of business. Pursuant to applicable accounting rules, we accrue the minimum liability for each known claim when the estimated outcome is a range of possible loss and no one amount within that range is more likely than another. We maintain insurance policies for such matters, and we record insurance recoveries when we determine such recovery to be probable. We do not expect any of these claims, individually or in the aggregate, to have a material adverse effect on our consolidated financial position or results of operations. We believe that the ultimate resolution of claims for any losses will not exceed our insurance policy coverages.

**Item 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

None.

**Executive Officers of the Registrant**

Executive officers are elected each year by the Board of Directors following the Annual Meeting of Shareholders to serve during the ensuing year and until their respective successors are elected and qualified. There are no family relationships between any of our executive officers or between any of them and any of the members of the Board of Directors.

The following information sets forth as of October 31, 2016, the name of each executive officer and his or her age, tenure as an officer, principal occupation and business experience:

<b>Name</b>	<b>Age</b>	<b>Position(s) with the Company</b>
Michael Doar	61	Chairman of the Board and Chief Executive Officer
Gregory S. Volovic	52	President
Sonja K. McClelland	45	Vice President, Secretary, Treasurer and Chief Financial Officer
John P. Donlon	59	Executive Vice President, International Sales/Service

Michael Doar was elected Chairman of the Board and Chief Executive Officer on November 14, 2001. Mr. Doar had held various management positions with Ingersoll Milling Machine Company from 1989 until 2001. Mr. Doar has been a director of Hurco since 2000.

Gregory S. Volovic has been employed by us since March 2005 and was elected as our President in March 2013. Mr. Volovic previously held the position of Executive Vice President, Software and Engineering until October 2009. Prior to joining us, Mr. Volovic held various positions with Thomson, Inc. including Director of E-Business, Engineering, and Information Technology. Prior to that, Mr. Volovic was employed by Unisys Corporation.

Sonja K. McClelland has been employed by us since September 1996 and was elected as Vice President, Secretary, Treasurer and Chief Financial Officer in March 2014. Ms. McClelland served as Corporate Accounting Manager from September 1996 to 1999, as Division Controller for Hurco USA from September 1999 to November 2004, and as our Corporate Controller and Assistant Secretary from November 2004 to March 2014. Prior to joining us, Ms. McClelland was employed for three years by an international public accounting firm.

John P. Donlon has been employed by us since April 2010 as Executive Vice President, International Sales/Service. Prior to joining us, Mr. Donlon served as the Vice President of Sales for Yaskawa America Robotics since 2008. From 2004 to 2008, Mr. Donlon served as the Vice President of Sales and Marketing for Ansaldo STS, a worldwide supplier of automation technologies to the rail industry. Earlier in his career, Mr. Donlon held executive sales and management positions with other multi-national companies including Honeywell and ABB, and he has significant international experience in the emerging markets of China, Russia and Brazil.

**PART II****Item 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES****Market Information**

Our common stock is traded on the Nasdaq Global Select Market under the symbol "HURC". The following table sets forth, for the periods indicated, the high and low sale prices as reported by the Nasdaq Global Select Market and declared dividends per share of our common stock.

Fiscal Quarter Ended:	2016			2015		
	High	Low	Declared Dividends	High	Low	Declared Dividends
January 31	\$28.47	\$23.90	\$ .08	\$39.95	\$30.33	\$ .07
April 30	\$33.40	\$23.25	\$ .09	\$38.37	\$28.22	\$ .08
July 31	\$33.65	\$26.57	\$ .09	\$35.77	\$30.13	\$ .08
October 31	\$30.42	\$25.45	\$ .09	\$31.80	\$24.93	\$ .08

On December 12, 2016, the closing price of our common stock on the Nasdaq Global Select Market was \$33.85.

**Holder**

There were 113 holders of record of our common stock as of December 12, 2016.

**Dividend Policy**

We began declaring cash dividends on our common stock in the third quarter of fiscal 2013, and we expect to continue to declare dividends on a quarterly basis; however, the declaration and amount of any future cash dividends will be subject to the sole discretion of our Board of Directors and will depend upon many factors, including our results of operations, financial condition, capital requirements, regulatory and contractual restrictions, our business strategy and other factors deemed relevant by our Board of Directors.

Our payment of dividends is limited by our U.S. credit agreement, as further described in Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations and in Note 5 of Notes to Consolidated Financial Statements.

**Other Information**

During the period covered by this report, we did not sell any equity securities that were not registered under the Securities Act of 1933, as amended.

The disclosure under the caption "Equity Compensation Plan Information" is incorporated by reference in Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters.

The performance graph information is included in Item 9B. Other Information.

**Item 6. SELECTED FINANCIAL DATA**

The Selected Financial Data presented below has been derived from our consolidated financial statements for the years indicated and should be read in conjunction with the consolidated financial statements and related notes set forth elsewhere herein and Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations.

	Year Ended October 31,				
	2016	2015	2014	2013	2012
	(In thousands, except per share amounts)				
Statement of Operations Data:					
Sales and service fees	\$227,289	\$219,383	\$222,303	\$192,804	\$203,117
Gross profit	70,440	69,091	68,612	55,056	63,181
Selling, general and administrative expenses	50,824	45,287	46,615	41,413	41,160
Operating income (loss)	19,616	23,804	21,997	13,643	22,021
Other income (expense)	(731 )	(251 )	(636 )	(1,201 )	(157 )
Net income (loss)	13,292	16,214	15,143	8,190	15,638
Earnings (loss) per common share- diluted	\$1.99	\$2.44	\$2.30	\$1.25	\$2.40
Weighted average common shares outstanding-diluted	6,642	6,602	6,538	6,497	6,470
Dividends declared per common share	\$.35	\$.31	\$.26	\$.10	—

	As of October 31,				
	2016	2015	2014	2013	2012
	(Dollars in thousands)				
Balance Sheet Data:					
Current assets *	\$218,381	\$216,112	\$208,691	\$182,921	\$172,200
Current liabilities	57,968	65,086	66,803	55,686	49,372
Working capital *	160,413	151,026	141,888	127,235	122,828
Current ratio *	3.8	3.3	3.1	3.3	3.5
Total assets *	251,949	248,577	239,176	212,804	197,360
Non-current liabilities *	8,506	8,923	7,728	5,627	4,194
Total debt	1,476	1,583	3,272	3,665	3,206
Shareholders' equity	185,475	174,568	164,645	151,491	143,793

\* Certain prior year amounts have been changed to conform to current year's presentation as a result of the adoption of Accounting Standards Update ("ASU") No. 2015-17.



**Item 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

**EXECUTIVE OVERVIEW**

Hurco Companies, Inc. is an international, industrial technology company operating in a single segment. We design, manufacture and sell computerized (i.e., Computer Numeric Control, or CNC) machine tools, consisting primarily of vertical machining centers (mills) and turning centers (lathes), to companies in the metal cutting industry through a worldwide sales, service and distribution network. Although the majority of our computer control systems and software products are proprietary, they predominantly use industry standard personal computer components. Our computer control systems and software products are primarily sold as integral components of our computerized machine tool products. We also provide machine tool components, software options, control upgrades, accessories and replacement parts for our products, as well as customer service and training support.

The following overview is intended to provide a brief explanation of the principal factors that have contributed to our recent financial performance. This overview is intended to be read in conjunction with the more detailed information included in our financial statements that appear elsewhere in this report.

The market for machine tools is international in scope. We have both significant foreign sales and significant foreign manufacturing operations. During fiscal 2016, approximately 54% of our revenues were attributable to customers in Europe, where we typically sell more of our higher-performance, higher-priced VMX series machines. Additionally, approximately 11% of our revenues were attributable to customers in Asia, where we sell more of our entry-level, lower-priced machines, but where we also encounter greater price pressures.

During the third quarter of fiscal 2015, we acquired the assets of the machine tool business of Milltronics Manufacturing Company, Inc. and we are operating this U.S. business as a product line through our wholly-owned subsidiary, Milltronics USA, Inc. ("Milltronics"). Milltronics manufactures and sells CNC knee mills, tool room bed mills, vertical machining centers, combination lathes, slant-bed lathes, horizontal machining centers, and bed mills. During the third quarter of fiscal 2015, we also acquired the assets of the machine tool business of Takumi Machinery Co., Ltd. ("Takumi"), a Taiwanese company that designs and manufactures CNC vertical machining centers, double column machining centers, high speed bridge machines and other machine tools, with sales primarily in Taiwan, China and Europe. Takumi machines are equipped with industrial controls from Fanuc®, Siemens®, Mitsubishi® or Heidenhain® which can be used in high-volume parts manufacturing. We are operating this Taiwanese business as a product line through our wholly-owned subsidiary Hurco Manufacturing Limited ("HML"). The Milltronics and Takumi product lines contribute to our efforts to expand our consolidated product range, customer base and global platform, and we believe may accelerate emerging market penetration, particularly in strategic markets such as China and South America. The Hurco, Milltronics and Takumi product lines represent a comprehensive product portfolio with more than 150 different models. The combined machine tool product lines also provide benefits related to the development

of product enhancements, technologies and models due to leverage of shared resources and cross-utilization of proven engineering designs that allow us to achieve manufacturing cost reductions from economies of scale and manufacturing efficiencies.

We sell our products through more than 195 independent agents and distributors throughout North and South America (the Americas), Europe and Asia. Although some distributors carry competitive products, we are the primary line for the majority of our distributors globally. We also have our own direct sales and service organizations in China, France, Germany, India, Italy, Poland, Singapore, South Africa, Taiwan, the United Kingdom and certain parts of the United States, which are among the world's principal machine tool consuming markets. The vast majority of our machine tools are manufactured to our specifications primarily by our wholly-owned subsidiary in Taiwan, HML. Machine castings and components to support HML's production are manufactured at our facility in Ningbo, China. Components to support our SRT line of five-axis machining centers, such as the direct drive spindle, swivel head and rotary table, are manufactured by our wholly-owned subsidiary in Italy, LCM Precision Technology S.r.l. ("LCM").

Our sales to foreign customers are denominated, and payments by those customers are made, in the prevailing currencies - primarily the Euro, Pound Sterling and Chinese Yuan - in the countries in which those customers are located. Our product costs are incurred and paid primarily in the New Taiwan Dollar and the Euro. Changes in currency exchange rates may have a material effect on our operating results and consolidated balance sheets as reported under U.S. Generally Accepted Accounting Principles. For example, when the U.S. Dollar weakens in value relative to a foreign currency, sales made, and expenses incurred, in that currency when translated to U.S. Dollars for reporting in our financial statements, are higher than would be the case when the U.S. Dollar is stronger. In the comparison of our period-to-period results, we discuss the effect of currency translation on those results, which reflect translation to U.S. Dollars at exchange rates prevailing during the period covered by those financial statements.

Our high levels of foreign manufacturing and sales also subject us to cash flow risks due to fluctuating currency exchange rates. We seek to mitigate those risks through the use of various derivative instruments – principally foreign currency forward exchange contracts.

### **Results of Operations**

The following table presents, for the fiscal years indicated, selected items from the Consolidated Statements of Income expressed as a percentage of our worldwide sales and service fees and the year-to-year percentage changes in the dollar amounts of those items.

	Percentage of Revenues			Year-to-Year % Change			
	2016	2015	2014	Increase/Decrease			
				'16 vs. '15	'15 vs. '14		
Sales and service fees	100 %	100 %	100 %	4	%	-1	%
Gross profit	31 %	31 %	31 %	2	%	1	%
Selling, general and administrative expenses	22 %	21 %	21 %	12	%	-3	%
Operating income (loss)	9 %	11 %	10 %	-18	%	8	%
Net income (loss)	6 %	7 %	7 %	-18	%	7	%

### **Fiscal 2016 Compared to Fiscal 2015**

*Sales and Service Fees.* Sales and service fees for fiscal 2016 were \$227.3 million, an increase of \$7.9 million, or 4%, compared to fiscal 2015 and included a negative currency impact of \$6.4 million, or 3%, when translating foreign sales to U.S. dollars for financial reporting purposes.

**Net Sales and Service Fees by Geographic Region**

The following table sets forth net sales and service fees by geographic region for the fiscal year ended October 31, 2016 and 2015 (in thousands):

	October 31,				Increase/Decrease			
	2016	2015	Amount	%		%		%
Americas	\$74,386	33 %	\$70,169	32 %	\$ 4,217	6 %		
Europe	124,070	54 %	129,335	59 %	(5,265 )	-4 %		
Asia Pacific	28,833	13 %	19,879	9 %	8,954	45 %		
Total	\$227,289	100 %	\$219,383	100 %	\$ 7,906	4 %		

Sales in the Americas for fiscal 2016 increased by 6% compared to fiscal 2015, as a result of year-end promotional activities following the International Manufacturing Technology Show (“IMTS”) in September 2016, as well as the impact of twelve months of Milltronics sales in fiscal 2016 compared to only three months of sales activity from the acquisition of the Milltronics product line in July 2015 until the end of fiscal 2015. Sales in the Americas for fiscal 2016 included \$17.9 million of sales from the Milltronics product line, compared to \$6.7 million in fiscal 2015. European sales for fiscal 2016 decreased by 4% compared to fiscal 2015 and included a negative currency impact of 5% when translating foreign sales to U.S. dollars for financial reporting purposes. The slight year-over-year growth in European sales for fiscal 2016, excluding the effect of the negative currency impact, was driven by increased shipments of higher-performance machines in Germany, France and Italy. Asian Pacific sales for fiscal 2016 increased by 45% compared to fiscal 2015 and included a negative currency impact of 3% when translating foreign sales to U.S. dollars for financial reporting purposes. The year-over-year increase in Asian Pacific sales for fiscal 2016 was primarily attributable to twelve months of Takumi sales included in fiscal 2016 compared to only three months of sales activity from the acquisition of the Takumi product line in July 2015 until the end of fiscal 2015. Asian Pacific sales for fiscal 2016 included \$14.6 million of sales from the Takumi product line, compared to \$3.3 million for fiscal 2015.

#### Net Sales and Service Fees by Product Category

The following table sets forth net sales and service fees by product group and services for the fiscal years ended October 31, 2016 and 2015 (in thousands):

	October 31,		Increase/ Decrease	
	2016	2015	Amount	%
Computerized Machine Tools*	\$195,618	86 % \$189,712	87 % \$5,906	3 %
Computer Control Systems and Software†	2,078	1 % 3,085	1 % (1,007)	-33 %
Service Parts	21,908	10 % 19,375	9 % 2,533	13 %
Service Fees	7,685	3 % 7,211	3 % 474	7 %
Total	\$227,289	100 % \$219,383	100 % \$7,906	4 %

\* Amounts shown include sales of Milltronics and Takumi computerized machine tools to third parties since the respective dates of those acquisitions.

† Amounts shown do not include computer control systems and software sold as an integrated component of computerized machine systems.

Sales of computerized machine tools and service parts increased during fiscal 2016 by 3% and 13%, respectively, compared to fiscal 2015 primarily due to the impact of twelve months of Milltronics and Takumi sales in fiscal 2016 compared to only three months of sales activity from the acquisitions of the Milltronics and Takumi product lines in July 2015 until the end of fiscal 2015, as well as year-end promotional activities following the International Manufacturing Technology Show (“IMTS”) in September 2016. Sales of computer control systems and software decreased by 33% during fiscal 2016 compared to fiscal 2015 as a result of a reduction in sales for the Autobend® product line in the Americas and the United Kingdom. Service fees revenue increased during fiscal 2016 by 7% compared to fiscal 2015 primarily due to increased repair needs from customers in the Americas, the United Kingdom and France.

*Orders and Backlog.* Orders for fiscal 2016 were \$219.2 million, a decrease of \$4.0 million, or 2%, compared to fiscal 2015 and included a negative currency impact of \$6.5 million, or 3%, when translating foreign orders to U.S. dollars for financial reporting purposes. Orders in the Americas for fiscal 2016 were \$70.9 million, a decrease of \$1.1 million, or 1%, compared to fiscal 2015, reflecting an overall softer market and the impact of pricing pressures in this region, partially offset by the impact of twelve months of Milltronics sales in fiscal 2016 compared to only three months in fiscal 2015. Orders in the Americas for fiscal 2016 included \$15.7 million of orders from the Milltronics product line, compared to \$10.1 million in fiscal 2015, of which approximately \$3.9 million of orders were existing backlog orders acquired with the Milltronics product line in July 2015. European orders for fiscal 2016 were \$121.5 million, a decrease of \$5.0 million, or 4%, compared to fiscal 2015, primarily due to the negative impact of currency when translating foreign orders to U.S. dollars for financial reporting purposes. Asian Pacific orders for fiscal 2016 were \$26.8 million, an increase of \$2.1 million, or 9%, compared to fiscal 2015 and included a negative currency impact of \$1.1 million, or 5%, when translating foreign orders to U.S. dollars for financial reporting purposes. The year-over-year increase in Asian Pacific orders were due primarily to increased customer demand for the Takumi product line in China. Asian Pacific orders for fiscal 2016 included \$12.7 million of orders from the Takumi product line, compared to \$10.6 million in fiscal 2015, of which approximately \$8.6 million of orders were existing backlog orders acquired with the Takumi product line in July 2015.

Backlog was \$32.3 million at October 31, 2016 compared to \$41.2 million at October 31, 2015. We do not believe backlog is a useful measure of past performance or indicative of future performance. Backlog orders as of October 31, 2016 are expected to be fulfilled in fiscal 2017.

*Gross Profit.* Gross profit for fiscal 2016 was \$70.4 million, or 31% of sales, which was consistent with gross profit for fiscal 2015 of \$69.1 million, or 31% of sales.

*Operating Expenses.* Selling, general and administrative expenses for fiscal 2016 were \$50.8 million, or 22% of sales, compared to \$45.3 million, or 21% of sales, for fiscal 2015. The year-over-year increase in operating expenses for fiscal 2016 was primarily due to increased trade show expenses, increased employee support costs for global sales operations, and incremental annualized operating expenses associated with the acquisitions of the Milltronics and Takumi product lines since July 2015.

*Operating Income.* Operating income for fiscal 2016 was \$19.6 million, or 9% of sales, compared to \$23.8 million, or 11% of sales, in fiscal 2015. The year-over-year reduction in operating income was primarily attributable to increased operating expenses associated with increased trade show expenses, increased employee support costs for global sales operations, and incremental operating expenses associated with the acquisitions of the Milltronics and Takumi product lines since July 2015.

*Other Expense, Net.* Other expense, net for fiscal 2016 increased by \$0.5 million from fiscal 2015 due mainly to higher foreign currency losses experienced in 2016 and the elimination of a one-time out-of-period income adjustment recorded in fiscal 2015.

*Provision for Income Taxes.* Our effective tax rate for fiscal 2016 was 30% in comparison to 31% for fiscal 2015. The decrease in the effective income tax rate for fiscal 2016 was due primarily to changes in the geographic mix of income or loss among tax jurisdictions.

*Net Income.* Net income for fiscal 2016 was \$13.3 million, or \$1.99 per diluted share, a decrease of \$2.9 million, or 18%, from fiscal 2015 net income of \$16.2 million, or \$2.44 per diluted share.

#### Fiscal 2015 Compared to Fiscal 2014

*Sales and Service Fees.* Sales and service fees for fiscal 2015 were \$219.4 million, a decrease of \$2.9 million, or 1%, compared to fiscal 2014 and included a negative currency impact of \$21.2 million, or 10%, compared to fiscal 2014. Sales for fiscal 2015 included \$10.0 million of sales activities from the acquisitions of the Takumi and Milltronics product lines in July 2015 until the end of fiscal 2015.

#### **Net Sales and Service Fees by Geographic Region**

The following table sets forth net sales and service fees by geographic region for the fiscal years ended October 31, 2015 and 2014 (in thousands):

	October 31,		2014		Increase/Decrease	
	2015				Amount	%
Americas	\$70,169	32 %	\$62,142	28 %	\$ 8,027	13 %
Europe	129,335	59 %	138,201	62 %	(8,866 )	-6 %
Asia Pacific	19,879	9 %	21,960	10 %	(2,081 )	-9 %
Total	\$219,383	100 %	\$222,303	100 %	\$ (2,920 )	-1 %

Sales in the Americas increased during fiscal 2015 by 13% compared to fiscal 2014 primarily due to three months of sales activity from the acquisition of the Milltronics product line in July 2015 until the end of fiscal 2015. Sales for the Milltronics product line in the Americas for fiscal 2015 were \$6.7 million. European sales for fiscal 2015 decreased by 6% compared to fiscal 2014 and included a negative currency impact of 14%. Excluding the negative currency impact, the year-over-year growth in European sales was driven by increased shipments of higher-performance machines in Germany, France and Italy. Asian Pacific sales for fiscal 2015 decreased by 9% compared to fiscal 2014, primarily due to softer markets in China and India and the negative impact of currency. Asian Pacific sales for fiscal 2015 included \$3.3 million of sales activity from the acquisition of the Takumi product line in July 2015 until the end of fiscal 2015.

#### Net Sales and Service Fees by Product Category

The following table sets forth net sales and service fees by product group and services for the fiscal years ended October 31, 2015 and 2014 (in thousands):

	October 31,		2014		Increase/Decrease	
	2015				Amount	%
Computerized Machine Tools*	\$189,712	87 %	\$193,937	87 %	\$ (4,225 )	-2 %
Computer Control Systems and Software†	3,085	1 %	3,407	2 %	(322 )	-9 %
Service Parts	19,375	9 %	17,391	8 %	1,984	11 %
Service Fees	7,211	3 %	7,568	3 %	(357 )	-5 %
Total	\$219,383	100 %	\$222,303	100 %	\$ (2,920 )	-1 %

\* Amounts shown include sales of Milltronics and Takumi computerized machine tools to third parties since the respective dates of those acquisitions.

† Amounts shown do not include computer control systems and software sold as an integrated component of computerized machine systems.

Sales of computerized machine tools decreased during fiscal 2015 by 2% compared to fiscal 2014 and included a negative currency impact of 9% when translating foreign sales to U.S. dollars for financial reporting purposes. Excluding the negative currency impact, the year-over-year increase in computerized machine tools was due to

increased shipments of higher-performance machines in Germany and France, as well as the impact of three months of sales activity from the acquisitions of the Milltronics and Takumi product lines in July 2015 until the end of fiscal 2015. Sales of computer control systems and software decreased by 9% during fiscal 2015 compared to fiscal 2014 due primarily to decreased shipments of Autobend® press brake machines and optional software products in the Americas. Sales of service parts increased by 11% during fiscal 2015 compared to fiscal 2014 due mainly to three months of sales activity from the acquisitions of the Milltronics and Takumi product lines in July 2015 until the end of fiscal 2015. Service fees revenue for fiscal 2015 decreased by 5% compared to fiscal 2014 primarily due to the negative impact of currency when translating foreign sales to U.S. dollars for financial reporting purposes.

*Orders and Backlog.* Orders for fiscal 2015 were \$223.2 million, a decrease of \$9.3 million, or 4%, compared to fiscal 2014 and included a negative currency impact of \$21.2 million, or 9%, when translating foreign orders into U.S. dollars for financial reporting purposes. Orders in the Americas for fiscal 2015 were \$72.0 million, an increase of \$8.6 million, or 14%, compared to fiscal 2014. Orders in the Americas for fiscal 2015 included \$10.1 million of orders related to the Milltronics product line. Excluding the orders related to the Milltronics product line, orders for the Americas decreased during fiscal 2015 compared to fiscal 2014 since promotional activities related to the International Manufacturing Technology Show held in September 2014 led to an increase in orders in fiscal 2014. European orders for fiscal 2015 were \$126.5 million, a decrease of \$22.0 million, or 15%, compared to fiscal 2014 and included a negative currency impact of \$20.4 million, or 14%. Excluding the negative impact of currency, the slight year-over-year reduction in European orders was primarily driven by foreign currency weakness in the United Kingdom and fluctuating customer demand for electro-mechanical components and accessories manufactured by LCM. Asian Pacific orders for fiscal 2015 were \$24.7 million, an increase of \$4.1 million, or 20%, compared to fiscal 2014. Asian Pacific orders for fiscal 2015 included \$10.6 million of orders related to the Takumi product line. Excluding the orders related to the Takumi product line, Asian Pacific orders for fiscal 2015 decreased primarily due to softer market conditions in China and India.

Backlog was \$41.2 million at October 31, 2015 (which included \$10.6 million of backlog for Milltronics and Takumi products) compared to \$39.8 million at October 31, 2014. We do not believe backlog is a useful measure of past performance or indicative of future performance.

*Gross Profit.* Gross profit for fiscal 2015 was \$69.1 million, or 31% of sales, compared to \$68.6 million, or 31% of sales, for fiscal 2014. The year-over-year improvement in gross profit was primarily attributable to increased sales of higher-performance machines across all regions, net of the pricing pressure and the negative impact of currency.

*Operating Expenses.* Selling, general and administrative expenses for fiscal 2015 were \$45.3 million, or 21% of sales, compared to \$46.6 million, or 21% of sales, for fiscal 2014. Fiscal year 2015 expenses included approximately \$2.4 million related to Milltronics and Takumi, of which \$0.7 million represented one-time acquisition costs. Selling, general and administrative expenses for fiscal 2015 included a positive impact of approximately \$3.2 million, or 1% of sales, when translating foreign expenses to U.S. dollars for financial reporting purposes.

*Operating Income.* Operating income for fiscal 2015 was \$23.8 million, or 11% of sales, compared to \$22.0 million, or 10% of sales, in fiscal 2014. The year-over-year improvement in operating income was primarily attributable to increased sales of higher-performance machines across all regions.

*Other Expense, Net.* Other expense, net for fiscal 2015 decreased by \$0.4 million from fiscal 2014 as a result of a one-time out-of-period income adjustment recorded in fiscal 2015.

*Provision for Income Taxes.* Our effective tax rate for fiscal 2015 was 31% in comparison to 29% for fiscal 2014. The increase in the effective income tax rate in fiscal 2015 was due primarily to changes in the geographic mix of income or loss among tax jurisdictions.

*Net Income.* Net income for fiscal 2015 was \$16.2 million, or \$2.44 per diluted share, an increase of \$1.1 million, or 7%, from fiscal 2014 net income of \$15.1 million, or \$2.30 per diluted share.

### **Liquidity and Capital Resources**

At October 31, 2016, we had cash and cash equivalents of \$41.2 million compared to \$55.2 million at October 31, 2015. Approximately 54% of our \$41.2 million of cash and cash equivalents is held in the U.S. The balance is attributable to our foreign operations and is held in the local currencies of our various foreign entities, subject to fluctuations in currency exchange rates. We do not believe that the indefinite reinvestment of these funds offshore impairs our ability to meet our domestic working capital needs.

Working capital (including cash and cash equivalents) was \$160.4 million at October 31, 2016 compared to \$151.0 million at October 31, 2015. The increase in working capital was primarily due to increased inventories, which were \$117.0 million at October 31, 2016, compared to \$106.3 million at October 31, 2015. The increase in inventories was primarily due to a reduction in orders during fiscal 2016, as well as incremental computerized machine tools for the Milltronics and Takumi product lines, which contributed to our efforts in expanding our consolidated product range to meet customers' needs. Inventory turns at October 31, 2016 were 1.4 compared to 1.6 turns at October 31, 2015.

Capital expenditures were \$4.2 million in fiscal 2016 compared to \$4.5 million in fiscal 2015. Capital expenditures for fiscal 2016 were primarily for software development costs, purchases of factory equipment for production facilities, and purchases of general software and equipment for selling facilities. We funded these expenditures with cash flows from operations.

On December 6, 2016, we amended our U.S. credit agreement, among other things, to increase the unsecured revolving credit facility from \$12.5 million to \$15.0 million, to increase the cash dividend allowance from \$4.0 million per calendar year to \$5.0 million per calendar year, and to extend the scheduled maturity date to December 31, 2018. We also amended the U.S. credit agreement to increase the minimum working capital and minimum tangible net worth requirements from \$90.0 million to \$105.0 million and \$120.0 million to \$125.0 million, respectively.

Borrowings under the U.S. credit agreement bear interest either at a LIBOR-based rate or a floating rate, in each case with an interest rate floor of 0.00%. The floating rate equals the greatest of (a) a one month LIBOR-based rate plus 1.00% per annum, (b) the federal funds effective rate plus 0.50% per annum, (c) the prevailing prime rate, and (d) 0.00%. The rate paid for the unutilized portion of the U.S. credit agreement is 0.05% per annum.

The U.S. credit agreement contains customary financial covenants, including covenants (1) restricting us from making certain investments, loans, advances and acquisitions (but permitting us to make investments in subsidiaries of up to \$5.0 million), (2) requiring that we maintain a minimum working capital of \$105.0 million, and (3) requiring that we maintain a minimum tangible net worth of \$125.0 million. The U.S. credit agreement permits us to pay cash dividends in an amount not to exceed \$5.0 million per calendar year, so long as we are not in default before and after giving effect to such dividends.

We have a £1.0 million revolving credit facility in England and a €1.5 million revolving credit facility in Germany. We also have a 40.0 million Chinese Yuan (approximately \$5.9 million) credit facility in China that was renewed on February 17, 2016 with an expiration date of February 16, 2017.

At October 31, 2016, we had \$1.5 million of borrowings under our China credit facility. We had no other debt or borrowings under any of our other credit facilities. At October 31, 2016, we were in compliance with the covenants contained in all of our credit facilities and had \$19.8 million of available borrowing capacity under those facilities.

We believe our cash position and borrowing capacity under our credit facilities provides adequate liquidity to fund our operations over the next twelve months, pay quarterly cash dividends and execute our strategic plan for product innovation and targeted penetration of developing markets.

We continue to receive and review information concerning businesses and assets , including intellectual property assets, available for potential acquisition.

Contractual Obligations and Commitments

The following is a table of contractual obligations and commitments as of October 31, 2016 (in thousands):

	Payments Due by Period				
	Total	Less than 1 Year	1-3 Years	3-5 Years	More than 5 Years
Short-term debt	\$1,476	\$1,476	\$—	\$—	\$—
Operating leases	6,347	2,930	2,485	589	343
Other...	4,212	—	963	—	3,249
Total	\$12,035	\$4,406	\$3,448	\$ 589	\$3,592

In addition to the contractual obligations and commitments disclosed above, we also have a variety of other obligations for the procurement of materials and services, none of which subject us to any material non-cancelable commitments. While some of these obligations arise under long-term supply agreements, we are not committed under these agreements to accept or pay for requirements that are not needed to meet our production needs. We have no material minimum purchase commitments or “take-or-pay” type agreements or arrangements. Unrecognized tax benefits in the amount of approximately \$1.1 million, excluding any interest and penalties, have been excluded from the table above because we are unable to determine a reasonably reliable estimate of the timing of future payment.

We expect capital spending in fiscal 2017 to be approximately \$5.9 million, which includes investments for capitalized software and capital equipment for all of our production and selling facilities. We expect to fund these commitments with cash on hand and cash generated from operations.

Off Balance Sheet Arrangements

From time to time, our subsidiaries guarantee third party payment obligations in connection with the sale of machines to customers that use financing. We follow Financial Accounting Standards Board (“FASB”) guidance for accounting for guarantees (codified in Accounting Standards Codification (“ASC”) 460). As of October 31, 2016, we had 26 outstanding third party payment guarantees totaling approximately \$1.2 million. The terms of these guarantees are consistent with the underlying customer financing terms. Upon shipment of a machine, the customer has the risk of ownership. The customer does not obtain title, however, until it has paid for the machine. A retention of title clause allows us to recover the machine if the customer defaults on the financing. We accrue liabilities under these guarantees at fair value, which amounts are insignificant.

### **Critical Accounting Policies and Estimates**

Our discussion and analysis of financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with U.S. Generally Accepted Accounting Principles. The preparation of financial statements in conformity with those accounting principles require us to make judgments and estimates that affect the amounts reported in the consolidated financial statements and accompanying notes. Those judgments and estimates have a significant effect on the financial statements because they result primarily from the need to make estimates about the effects of matters that are inherently uncertain. Actual results could differ from those estimates. Our accounting policies, including those described below, are frequently evaluated as our judgment and estimates are based upon historical experience and on various other assumptions that are believed to be reasonable under the circumstances.

*Revenue Recognition* - We recognize revenue from sales of our machine tool systems upon delivery of the product to the customer, which is normally at the time of shipment, because persuasive evidence of an arrangement exists, delivery has occurred, the selling price is fixed and determinable and collectability is reasonably assured. Our computerized machine tools are general-purpose computer controlled machine tools that are typically used in stand-alone operations. Transfer of ownership and risk of loss are not contingent upon contractual customer acceptance. Prior to shipment, we test each machine to ensure the machine's compliance with standard operating specifications.

Depending upon geographic location, after shipment, a machine may be installed at the customer's facilities by a distributor, independent contractor or by one of our service technicians. In most instances where a machine is sold through a distributor, we have no installation involvement. If sales are direct or through sales agents, we will typically complete the machine installation, which consists of the reassembly of certain parts that were removed for shipping and the re-testing of the machine to ensure that it is performing within the standard specifications. We consider the machine installation process to be inconsequential and perfunctory.

Service fees from maintenance contracts are deferred and recognized in earnings on a pro rata basis over the term of the contract. Sales related to software products are recognized when shipped in conformity with U.S. Generally Accepted Accounting Principles as promulgated by FASB related to software revenue recognition that requires at the time of shipment, persuasive evidence of an arrangement exists, delivery has occurred, the selling price is fixed and determinable and collectability is reasonably assured. The software does not require production, modification or customization.

*Inventories* – We determine at each balance sheet date how much, if any, of our inventory may ultimately prove to be either unsalable or unsalable at its carrying cost. Reserves are established to effectively adjust the carrying value of such inventory to net realizable value. To determine the appropriate level of valuation reserves, we evaluate current stock levels in relation to historical and expected patterns of demand for all of our products. We evaluate the need for changes to valuation reserves based on market conditions, competitive offerings and other factors on a regular basis.

*Income Taxes* – We account for income taxes and the related accounts under the asset and liability method. Deferred tax assets and liabilities are measured using enacted income tax rates in each jurisdiction in effect for the year in which the temporary differences are expected to be recovered or settled. These deferred tax assets are reduced by a valuation allowance, which is established when it is more likely than not that some portion or all of the deferred tax assets will not be realized. Our judgment regarding the realization of deferred tax assets may change due to future profitability and market conditions, changes in U.S. or foreign tax laws and other factors. These changes, if any, may require material adjustments to these deferred tax assets and an accompanying reduction or increase in net income in the period when such determinations are made.

The determination of our provision for income taxes requires judgment, the use of estimates and the interpretation and application of complex tax laws. Our provision for income taxes reflects a combination of income earned and taxed at the federal and state level in the U.S., as well as in various foreign jurisdictions. We have not provided for any U.S. income taxes on the undistributed earnings of our foreign subsidiaries based upon our determination that such earnings will be indefinitely reinvested abroad. Undistributed earnings of our wholly-owned foreign subsidiaries at October 31, 2016 were approximately \$79.7 million. In the event these earnings are later distributed to the U.S., such distributions would likely result in additional U.S. tax that may be offset, at least in part, by associated foreign tax credits.

In addition to the risks to the effective tax rate described above, the future effective tax rate reflected in forward-looking statements is based on currently effective tax laws. Significant changes in those laws could materially affect these estimates.

We recognize uncertain tax positions when it is more likely than not that the tax position will be sustained upon examination by relevant taxing authorities, based on the technical merits of the position. The amount recognized is measured as the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement.

*Impairment of Long-Lived Assets* – We are required periodically to review the recoverability of certain assets, including property, plant and equipment, intangible assets and goodwill, based on projections of anticipated future cash flows, including future profitability assessments of various product lines. We estimate cash flows using internal budgets based on recent sales data.

*Capitalized Software Development Costs* – Costs incurred to develop computer software products and significant enhancements to software features of existing products are capitalized as required by FASB guidance relating to accounting for the costs of computer software to be sold, leased, or otherwise marketed, and such capitalized costs are amortized over the estimated product life of the related software. The determination as to when in the product development cycle technological feasibility has been established, and the expected product life, require judgments and estimates by management and can be affected by technological developments, innovations by competitors and changes in market conditions affecting demand. We periodically review the carrying values of these assets and make judgments as to ultimate realization considering the above-mentioned risk factors.

*Derivative Financial Instruments* – Critical aspects of our accounting policy for derivative financial instruments that we designate as hedging instruments include conditions that require that critical terms of a hedging instrument are essentially the same as a hedged forecasted transaction. Another important element of our policy demands that formal documentation be maintained as required by FASB guidance relating to accounting for derivative instruments and hedging activities. Failure to comply with these conditions would result in a requirement to recognize changes in market value of hedge instruments in earnings. We routinely monitor significant estimates, assumptions, and judgments associated with derivative instruments, and compliance with formal documentation requirements.

*Stock Compensation* – We account for share-based compensation according to FASB guidance relating to share-based payments, which requires the measurement and recognition of compensation expense for all share-based awards made to employees and directors based on estimated fair values on the grant date. This guidance requires that we estimate the fair value of share-based awards on the date of grant and recognize as expense the value of the portion of the award that is ultimately expected to vest over the requisite service period.

**Item 7A. Quantitative and Qualitative Disclosures About Market Risk**

**Interest Rate Risk**

Interest on borrowings under our bank credit agreements are tied to prevailing domestic and foreign interest rates. At October 31, 2016, we had \$1.5 million of borrowings under our China credit facility. We had no other debt or borrowings under any of our other credit facilities.

**Foreign Currency Exchange Risk**

In fiscal 2016, we derived approximately 69% of our revenues from customers located outside of the U.S. All of our computerized machine tools and computer control systems assembled in Taiwan, as well as certain proprietary service parts, are sourced by our U.S.-based engineering and manufacturing division and re-invoiced to our foreign sales and service subsidiaries, primarily in their functional currencies.

Our products are sourced from foreign suppliers or built to our specifications by either our wholly-owned subsidiaries in Taiwan, U.S., Italy and China or an affiliated contract manufacturer in Taiwan. Our purchases are predominantly in foreign currencies and in some cases our arrangements with these suppliers include foreign currency risk sharing agreements, which reduce (but do not eliminate) the effects of currency fluctuations on product costs. The predominant portion of the exchange rate risk associated with our product purchases relates to the New Taiwan Dollar and the Euro.

We enter into foreign currency forward exchange contracts from time to time to hedge the cash flow risk related to forecasted inter-company sales and purchases denominated in, or based on, foreign currencies (primarily the Euro, Pound Sterling, and New Taiwan Dollar). We also enter into foreign currency forward exchange contracts to protect against the effects of foreign currency fluctuations on receivables and payables denominated in foreign currencies. We do not speculate in the financial markets and, therefore, do not enter into these contracts for trading purposes.

Forward contracts for the sale or purchase of foreign currencies as of October 31, 2016, which are designated as cash flow hedges under FASB guidance related to accounting for derivative instruments and hedging activities, were as follows:

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<b>Forward</b>	<b>Notional Amount in Foreign Currency</b>	<b>Weighted Avg. Forward Rate</b>	<b>Contract Amount at Forward Rates in U.S. Dollars</b>			<b>Maturity Dates</b>
			<b>Contract Date</b>	<b>October 31, 2016</b>	<b>Contract</b>	
<b>Contracts</b>						
<b>Sale Contracts:</b>						
Euro	25,000,000	1.1202	\$ 28,004,935	\$ 27,600,641		Nov 2016-Oct 2017
Sterling	4,925,000	1.3934	\$ 6,862,675	\$ 6,050,529		Nov 2016-Oct 2017
<b>Purchase Contracts:</b>						
New Taiwan Dollar	685,000,000	32.07	* \$ 21,361,677	\$ 21,753,310		Nov 2016-Oct 2017

\*NT Dollars per U.S. Dollar

Forward contracts for the sale or purchase of foreign currencies as of October 31, 2016, which were entered into to protect against the effects of foreign currency fluctuations on receivables and payables and are not designated as hedges under this guidance denominated in foreign currencies, were as follows:

<b>Forward Contracts</b>	<b>Notional Amount in Foreign Currency</b>	<b>Weighted Avg. Forward Rate</b>	<b>Contract Date</b>	<b>Contract Amount at Forward Rates in U.S. Dollars October 31, 2016</b>		<b>Maturity Dates</b>
<b>Sale Contracts:</b>						
Euro	33,047,215	1.0998	\$ 36,346,017	\$ 36,469,657		Nov 2016-Apr 2017
Pound Sterling	1,634,180	1.2162	\$ 1,987,522	\$ 2,003,054		Nov 2016-Dec 2016
South African Rand	14,831,600	0.0698	\$ 1,034,522	\$ 1,062,494		Apr 2017
<b>Purchase Contracts:</b>						
New Taiwan Dollar	838,537,514	31.32	* \$ 26,769,329	\$ 26,593,682		Nov 2016-Feb 2017

\* NT Dollars per U.S. Dollar

We are exposed to foreign currency exchange risk related to our investment in net assets in foreign countries. To manage this risk, we entered into a forward contract with a notional amount of €3.0 million in November 2015. We designated this forward contract as a hedge of our net investment in Euro denominated assets. We selected the forward method under the FASB guidance related to the accounting for derivatives instruments and hedging activities. The forward method requires all changes in the fair value of the contract to be reported as a cumulative translation adjustment in Accumulated Other Comprehensive Loss, net of tax, in the same manner as the underlying hedged net assets. This forward contract matured in November 2016 and we entered into a new forward contract for the same notional amount that is set to mature in November 2017. As of October 31, 2016, we had a realized gain of \$803,000 and an unrealized loss of \$39,000, net of tax, recorded as cumulative translation adjustments in Accumulated other comprehensive loss, related to these forward contracts.

Forward contracts for the sale or purchase of foreign currencies as of October 31, 2016, which are designated as net investment hedges under this guidance were as follows:

<b>Forward Contracts</b>	<b>Notional Amount in Foreign Currency</b>	<b>Weighted Avg. Forward Rate</b>	<b>Contract Date</b>	<b>Contract Amount at Forward Rates in U.S. Dollars October 31, 2016</b>		<b>Maturity Date</b>
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Sale Contracts:

Euro	3,000,000	1.0775	\$ 3,232,500	\$ 3,292,170	Nov 2016
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## **Management’s Annual Report on Internal Control Over Financial Reporting**

To the Shareholders and  
Board of Directors  
of Hurco Companies, Inc.

Management of Hurco Companies, Inc. (the “Company”) has assessed the effectiveness of the Company’s internal control over financial reporting as of October 31, 2016, based on criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 framework) (COSO). Management is responsible for these financial statements, for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting.

Because of its inherent limitations, the Company’s internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In management’s opinion, the Company’s internal control over financial reporting as of October 31, 2016, was effective based on the criteria specified above.

Our independent registered accounting firm, Ernst & Young LLP, who also audited our consolidated financial statements, audited the effectiveness of our internal control over financial reporting as of October 31, 2016. Ernst & Young has issued their attestation report, which is included in Part II, Item 8 of this Annual Report on Form 10-K.

/s/ Michael Doar  
Michael Doar,  
Chairman of the  
Board and Chief  
Executive Officer

/s/ Sonja K. McClelland  
Sonja K. McClelland

Vice President,  
Secretary, Treasurer and  
Chief Financial Officer

Indianapolis, Indiana

January 6, 2017

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**Item 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA**

Report of Independent Registered Public Accounting Firm

To the Shareholders and

Board of Directors

of Hurco Companies, Inc.

We have audited the accompanying consolidated balance sheets of Hurco Companies, Inc. as of October 31, 2016 and 2015 and the related consolidated statements of income, comprehensive income, changes in shareholders' equity and cash flows for each of the three years in the period ended October 31, 2016. Our audits also included the financial statement schedule listed at Item 15(a). These financial statements and schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and 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. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes 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, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Hurco Companies, Inc. at October 31, 2016 and 2015 and the consolidated results of its operations and its cash flows for each of the three years in the period ended October 31, 2016 in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic financial statements taken as a whole, presents fairly in all material respects the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Hurco Companies, Inc.'s internal control over financial reporting as of October 31, 2016, based on criteria established in Internal Control – Integrated Framework issued by the Commission of Sponsoring Organizations of the Treadway Commission (2013 framework) and our report dated January 6, 2017 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Indianapolis, Indiana

January 6, 2017

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**Report of Independent Registered Public Accounting Firm**

To the Shareholders and  
Board of Directors  
of Hurco Companies, Inc.

We have audited Hurco Companies, Inc.'s internal control over financial reporting as of October 31, 2016, based on criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (2013 Framework) (the COSO criteria). Hurco Companies, Inc.'s management is responsible for maintaining effective internal control over financial reporting, and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Annual Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the company's internal control over financial reporting based on our audit.

We conducted our audit 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 effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become

inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Hurco Companies, Inc. maintained, in all material respects, effective internal control over financial reporting as of October 31, 2016, based on the COSO criteria.

We have also audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Hurco Companies, Inc. as of October 31, 2016 and 2015 and the related consolidated statements of income, comprehensive income, changes in shareholders' equity and cash flows for each of the three years in the period ended October 31, 2016 of Hurco Companies, Inc. and our report dated January 6, 2017 expressed an unqualified opinion thereon.

/s/ Ernst & Young LLP

Indianapolis, Indiana

January 6, 2017

**HURCO COMPANIES, INC.****CONSOLIDATED STATEMENTS OF INCOME**

	Year Ended October 31,		
	2016	2015	2014
	(In thousands, except per share amounts)		
Sales and service fees	\$ 227,289	\$ 219,383	\$ 222,303
Cost of sales and service	156,849	150,292	153,691
Gross profit	70,440	69,091	68,612
Selling, general and administrative expenses	50,824	45,287	46,615
Operating income	19,616	23,804	21,997
Interest expense	72	198	264
Interest income	40	76	78
Investment income	149	78	42
Income from equity investments	466	474	444
Other expense, net	1,314	681	936
Income before income taxes	18,885	23,553	21,361
Provision for income taxes	5,593	7,339	6,218
Net income	\$ 13,292	\$ 16,214	\$ 15,143
Income per common share – basic	\$ 2.01	\$ 2.46	\$ 2.31
Weighted average common shares outstanding – basic	6,569	6,543	6,497
Income per common share – diluted	\$ 1.99	\$ 2.44	\$ 2.30
Weighted average common shares outstanding – diluted	6,642	6,602	6,538
Dividends paid per share	\$ .35	\$ .31	\$ .26

*The accompanying notes are an integral part of the consolidated financial statements.*

**HURCO COMPANIES, INC.****CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME**

	Year Ended October 31,		
	2016	2015	2014
	(In thousands)		
Net Income	\$13,292	\$16,214	\$15,143
Other comprehensive income (loss):			
Translation gain (loss) of foreign currency financial statements	(1,441 )	(6,333 )	(3,535 )
(Gain) / loss on derivative instruments reclassified into operations, net of tax of \$(906), \$(431), and \$621, respectively	(1,647 )	(784 )	1,129
Gain / (loss) on derivative instruments, net of tax of \$787, \$712, and \$458, respectively	1,431	1,291	830
Total other comprehensive income (loss)	(1,657 )	(5,826 )	(1,576 )
Comprehensive income	\$11,635	\$10,388	\$13,567

*The accompanying notes are an integral part of the consolidated financial statements.*

**HURCO COMPANIES, INC.****CONSOLIDATED BALANCE SHEETS**

	As of October 31,	
	2016	2015
	(In thousands, except share and per share data)	
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 41,217	\$ 55,237
Accounts receivable, less allowance for doubtful accounts of \$664 in 2016 and \$739 in 2015	48,631	41,766
Inventories, net	117,025	106,308
Derivative assets	1,725	1,228
Prepaid assets	8,207	9,769
Other	1,576	1,804
Total current assets	218,381	216,112
Property and equipment:		
Land	841	841
Building	7,352	7,314
Machinery and equipment	23,515	24,026
Leasehold improvements	3,487	3,323
	35,195	35,504
Less accumulated depreciation and amortization	(22,898)	(22,362)
Total property and equipment, net	12,297	13,142
<b>Non-current assets:</b>		
Software development costs, less accumulated amortization	4,926	3,905
Goodwill	2,314	2,319
Intangible assets, net	1,150	1,289
Deferred income taxes	6,138	4,721
Investments and other assets, net	6,743	7,089
Total non-current assets	21,271	19,323
Total assets	\$ 251,949	\$ 248,577
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 35,210	\$ 41,678
Accounts payable-related parties	1,990	1,780
Accrued expenses and other	17,231	16,788
Accrued warranty expenses	1,523	2,186
Derivative liabilities	538	1,071
Short-term debt	1,476	1,583
Total current liabilities	57,968	65,086
Non-current liabilities:		

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Deferred income taxes	4,294	3,998
Accrued tax liability	963	953
Deferred credits and other	3,249	3,972
Total non-current liabilities	8,506	8,923
Shareholders' equity:		
Preferred stock: no par value per share, 1,000,000 shares authorized, no shares issued	—	—
Common stock: no par value, \$.10 stated value per share, 12,500,000 shares authorized, 6,720,453 and 6,650,517 shares issued; and 6,573,103 and 6,551,718 shares outstanding, as of October 31, 2016 and October 31, 2015, respectively	657	655
Additional paid-in capital	59,119	57,539
Retained earnings	136,742	125,760
Accumulated other comprehensive loss	(11,043	) (9,386
Total shareholders' equity	185,475	174,568
Total liabilities and shareholders' equity	\$ 251,949	\$ 248,577

*The accompanying notes are an integral part of the consolidated financial statements.*

**HURCO COMPANIES, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS**

	Year Ended October 31,		
	2016	2015	2014
	(In thousands)		
Cash flows from operating activities:			
Net income	\$13,292	\$16,214	\$15,143
Adjustments to reconcile net income to net cash provided by (used for) operating activities, net of acquisitions:			
Provision for doubtful accounts	(75 )	(139 )	338
Deferred income taxes	(225 )	(1,013 )	(874 )
Equity in income of affiliates	(466 )	(474 )	(444 )
Foreign currency (gain) loss	1,850	3,223	2,260
Unrealized (gain) loss on derivatives	393	147	208
Depreciation and amortization	3,868	3,222	3,309
Stock-based compensation	1,607	1,193	921
Change in assets and liabilities, net of acquisitions:			
(Increase) decrease in accounts receivable	(8,141 )	3,666	(11,653)
(Increase) decrease in inventories	(13,881)	2,852	(4,971 )
(Increase) decrease in prepaid expenses	809	383	(4,646 )
Increase (decrease) in accounts payable	(6,001 )	(1,028 )	8,642
Increase (decrease) in accrued expenses	(90 )	(962 )	5,257
Net change in derivative assets and liabilities	(245 )	1,081	2,842
Other	442	179	3
Net cash provided by (used for) operating activities	(6,863 )	28,544	16,335
Cash flows from investing activities:			
Proceeds from sale of property and equipment	264	62	125
Purchase of property and equipment	(1,972 )	(3,127 )	(1,680 )
Software development costs	(2,205 )	(1,406 )	(955 )
Other investments	—	308	(76 )
Acquisition of business, net of cash acquired	—	(17,650)	—
Net cash provided by (used for) investing activities	(3,913 )	(21,813)	(2,586 )
Cash flows from financing activities:			
Proceeds from exercise of common stock options	—	257	359
Dividends paid	(2,310 )	(2,034 )	(1,693 )
Tax benefit from exercise of stock options	—	119	—
Repayment on short-term debt	—	(1,605 )	(379 )
Net cash provided by (used for) financing activities	(2,310 )	(3,263 )	(1,713 )
Effect of exchange rate changes on cash and cash equivalents	(934 )	(2,077 )	(994 )
Net increase (decrease) in cash and cash equivalents	(14,020)	1,391	11,042

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Cash and cash equivalents at beginning of year	55,237	53,846	42,804
Cash and cash equivalents at end of year	\$41,217	\$55,237	\$53,846
Supplemental disclosures:			
Cash paid for:			
Interest	\$56	\$156	\$167
Income taxes, net	\$4,328	\$9,890	\$5,782

*The accompanying notes are an integral part of the consolidated financial statements.*

**HURCO COMPANIES, INC.****CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY**

(In thousands, except shares outstanding)	<b>Common Stock  Shares Outstanding</b>	<b>Common Stock  Amount</b>	<b>Additional Paid-In Capital</b>	Retained Earnings	Accumulated Other Comprehensive Loss	Total
Balances, October 31, 2013	6,465,054	\$ 647	\$54,698	\$98,130	\$ (1,984 )	\$151,491
Net income	—	—	—	15,143	—	15,143
Other comprehensive income (loss)	—	—	—	—	(1,576 )	(1,576 )
Exercise of common stock options	20,306	2	357	—	—	359
Stock-based compensation expense	23,520	2	919	—	—	921
Dividends paid	—	—	—	(1,693 )	—	(1,693 )
Balances, October 31, 2014	6,508,880	\$ 651	\$55,974	\$111,580	\$ (3,560 )	\$164,645
Net income	—	—	—	16,214	—	16,214
Other comprehensive income (loss)	—	—	—	—	(5,826 )	(5,826 )
Exercise of common stock options	15,300	1	256	—	—	257
Stock-based compensation expense	27,538	3	1,190	—	—	1,193
Tax benefit (expense) from stock option activities	—	—	119	—	—	119
Dividends paid	—	—	—	(2,034 )	—	(2,034 )
Balances, October 31, 2015	6,551,718	\$ 655	\$57,539	\$125,760	\$ (9,386 )	\$174,568
Net income	—	—	—	13,292	—	13,292
Other comprehensive income (loss)	—	—	—	—	(1,657 )	(1,657 )
Stock-based compensation expense	21,385	2	1,605	—	—	1,607

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Tax benefit (expense) from stock option activities	—	—	(25 )	—	—	(25 )
Dividends paid	—	—	—	(2,310 )	—	(2,310 )
Balances, October 31, 2016	6,573,103	\$ 657	\$59,119	\$136,742	\$ (11,043 )	\$185,475

*The accompanying notes are an integral part of the consolidated financial statements.*

**HURCO COMPANIES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

*Consolidation.* The consolidated financial statements include the accounts of Hurco Companies, Inc. (an Indiana corporation) and its wholly-owned subsidiaries. We have a 35% ownership interest in a Taiwan affiliate that is accounted for using the equity method. Our investment in that affiliate was approximately \$3.6 million and \$3.0 million as of October 31, 2016 and 2015, respectively. That investment is included in Investments and other assets, net on the accompanying Consolidated Balance Sheets. Intercompany accounts and transactions have been eliminated.

*Statements of Cash Flows.* We consider all highly liquid investments with a stated maturity at the date of purchase of three months or less to be cash equivalents. Cash flows from hedges are classified consistent with the items being hedged.

*Translation of Foreign Currencies.* All balance sheet accounts of non-U.S. subsidiaries are translated at the exchange rate as of the end of the year and translation adjustments of foreign currency balance sheets are recorded as a component of Accumulated other comprehensive loss in shareholders' equity. Income and expenses are translated at the average exchange rates during the year. Cumulative foreign currency translation adjustments, net of gains related to our net investment hedges, as of October 31, 2016 were a net loss of \$12.3 million and are included in Accumulated other comprehensive loss. Foreign currency transaction gains and losses are recorded as income or expense as incurred and are recorded in Other expense, net.

*Hedging.* We are exposed to certain market risks relating to our ongoing business operations, including foreign currency risk, interest rate risk and credit risk. We manage our exposure to these and other market risks through regular operating and financing activities. Currently, the only risk that we manage through the use of derivative instruments is foreign currency risk.

We operate on a global basis and are exposed to the risk that our financial condition, results of operations and cash flows could be adversely affected by changes in foreign currency exchange rates. To reduce the potential effects of foreign exchange rate movements on our net equity investment in one of our foreign subsidiaries, and the gross profit and net earnings of certain of our foreign subsidiaries, we enter into derivative financial instruments in the form of foreign exchange forward contracts with a major financial institution. We are primarily exposed to foreign currency exchange rate risk with respect to transactions and net assets denominated in Euros, Pounds Sterling, Indian Rupee, South African Rand, Singapore Dollars, Chinese Yuan, Polish Zloty, and New Taiwan Dollars.

We account for derivative instruments as either assets or liabilities and carry them at fair value. The accounting for changes in the fair value of a derivative depends on the intended use of the derivative and the resulting designation. For derivative instruments designated as a fair value hedge, the gain or loss is recognized in earnings in the period of change together with the offsetting loss or gain on the hedged item attributed to the risk being hedged. For a derivative instrument designated as a cash flow hedge, the effective portion of the derivative's gain or loss is initially reported as a component of Accumulated other comprehensive loss in shareholders' equity and subsequently reclassified into earnings when the hedged exposure affects earnings. The ineffective portion of the gain or loss is reported in earnings immediately.

For derivative instruments that are not designated as accounting hedges under the Derivatives and Hedging Topic of the Financial Accounting Standards Board (FASB guidance), changes in fair value are recognized in earnings in the period of change. We do not hold or issue derivative financial instruments for speculative trading purposes. We only enter into derivatives with one counterparty, which is among one of the largest U.S. banks (ranked by assets), in order to minimize credit risk and, to date, that counterparty has not failed to meet its financial obligations under such contracts.

**HURCO COMPANIES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued**

Derivatives Designated as Hedging Instruments

We enter into foreign currency forward exchange contracts periodically to hedge certain forecasted inter-company sales and purchases denominated in foreign currencies (the Pound Sterling, Euro and New Taiwan Dollar). The purpose of these instruments is to mitigate the risk that the U.S. Dollar net cash inflows and outflows resulting from sales and purchases denominated in foreign currencies will be adversely affected by changes in exchange rates. These forward contracts have been designated as cash flow hedge instruments, and are recorded in the Consolidated Balance Sheets at fair value in Derivative assets and Derivative liabilities. The effective portion of the gains and losses resulting from the changes in the fair value of these hedge contracts are deferred in Accumulated other comprehensive loss and recognized as an adjustment to Cost of sales and service in the period that the corresponding inventory sold that is the subject of the related hedge contract is recognized, thereby providing an offsetting economic impact against the corresponding change in the U.S. Dollar value of the inter-company sale or purchase being hedged. The ineffective portion of gains and losses resulting from the changes in the fair value of these hedge contracts is reported in Other (income) expense, net immediately. We perform quarterly assessments of hedge effectiveness by verifying and documenting the critical terms of the hedge instrument and determining that forecasted transactions have not changed significantly. We also assess on a quarterly basis whether there have been adverse developments regarding the risk of a counterparty default.

We had forward contracts outstanding as of October 31, 2016, in Euros, Pounds Sterling and New Taiwan Dollars with set maturity dates ranging from November 2016 through October 2017. The contract amount at forward rates in U.S. Dollars at October 31, 2016 for Euros and Pounds Sterling was \$27.6 million and \$6.1 million, respectively. The contract amount at forward rates in U.S. Dollars for New Taiwan Dollars was \$21.8 million at October 31, 2016. At October 31, 2016, we had approximately \$1.3 million of gains, net of tax, related to cash flow hedges deferred in Accumulated other comprehensive loss. Of this amount, \$1.0 million represented unrealized gains, net of tax, related to cash flow hedge instruments that remain subject to currency fluctuation risk. The majority of these deferred gains will be recorded as an adjustment to Cost of sales and service in periods through October 2017, in which the corresponding inventory that is the subject of the related hedge contract is sold, as described above.

We are exposed to foreign currency exchange risk related to our investment in net assets in foreign countries. To manage this risk, we entered into a forward contract with a notional amount of €3.0 million in November 2015. We designated this forward contract as a hedge of our net investment in Euro denominated assets. We selected the forward method under the FASB guidance related to the accounting for derivatives instruments and hedging activities. The forward method requires all changes in the fair value of the contract to be reported as a cumulative translation adjustment in Accumulated other comprehensive loss, net of tax, in the same manner as the underlying hedged net assets. This forward contract matured in November 2016 and we entered into a new forward contract for the same

notional amount that is set to mature in November 2017. As of October 31, 2016, we had a realized gain of \$803,000 and an unrealized loss of \$39,000, net of tax, recorded as cumulative translation adjustments in Accumulated other comprehensive loss, related to these forward contracts.

#### Derivatives Not Designated as Hedging Instruments

We enter into foreign currency forward exchange contracts to protect against the effects of foreign currency fluctuations on receivables and payables denominated in foreign currencies. These derivative instruments are not designated as hedges under FASB guidance and, as a result, changes in their fair value are reported currently as Other expense, net in the Consolidated Statements of Income consistent with the transaction gain or loss on the related receivables and payables denominated in foreign currencies.

**HURCO COMPANIES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued**

We had forward contracts outstanding as of October 31, 2016, in Euros, Pounds Sterling, South African Rand and New Taiwan Dollars with set maturity dates ranging from November 2016 through April 2017. The contract amounts at forward rates in U.S. Dollars at October 31, 2016 for Euros, Pounds Sterling and South African Rand totaled \$39.5 million. The contract amount at forward rates in U.S. Dollars for New Taiwan Dollars was \$26.6 million at October 31, 2016.

Fair Value of Derivative Instruments

We recognize the fair value of derivative instruments as assets and liabilities on a gross basis on our Consolidated Balance Sheets. As of October 31, 2016 and October 31, 2015, all derivative instruments were recorded at fair value on the balance sheets as follows (in thousands):

Derivatives	2016		2015	
	Balance Sheet Location	Fair Value	Balance Sheet Location	Fair Value
Designated as Hedging Instruments:				
Foreign exchange forward contracts	Derivative assets	\$1,721	Derivative assets	\$1,079
Foreign exchange forward contracts	Derivative liabilities	\$173	Derivative liabilities	\$1,027
Not Designated as Hedging Instruments:				
Foreign exchange forward contracts	Derivative assets	\$4	Derivative assets	\$149
Foreign exchange forward contracts	Derivative liabilities	\$365	Derivative liabilities	\$44

Effect of Derivative Instruments on the Consolidated Balance Sheets, Statements of Changes in Shareholders' Equity and Statements of Income

Derivative instruments had the following effects on our Consolidated Balance Sheets, Statements of Changes in Shareholders' Equity and Statements of Income, net of tax, during the fiscal years ended October 31, 2016 and 2015 (in thousands):

Derivatives	Amount of Gain (Loss)		Location of Gain (Loss) Reclassified from Other Comprehensive Income (Loss)	Amount of Gain (Loss)	
	Recognized in Other Comprehensive Income (Loss)			Reclassified from Other Comprehensive Income (Loss)	
	2016	2015		2016	2015
<u>Designated as Hedging Instruments:</u>					
(Effective Portion)					
Foreign exchange forward contracts – Intercompany sales/purchases	\$ 1,431	\$ 1,291	Cost of sales and service	\$ 1,647	\$ 784
Foreign exchange forward contract – Net Investment	\$ 28	\$ 304			

**HURCO COMPANIES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued**

We recognized a gain of \$18,000 during the fiscal year ended October 31, 2016 and a gain of \$14,000 during the fiscal year ended October 31, 2015 as a result of contracts closed early that were deemed ineffective for financial reporting and did not qualify as cash flow hedges.

Derivatives	Location of Gain (Loss)	Amount of Gain (Loss)	
	Recognized in Operations	Recognized in Operations 2016	Recognized in Operations 2015
		(in thousands)	
Not Designated as Hedging Instruments:			
Foreign exchange forward contracts	Other expense, net	\$ 536	\$ 2,571

The following table presents the changes in the components of Accumulated other comprehensive loss, net of tax, for the fiscal years ended October 31, 2016 and 2015 (in thousands):

	Foreign Currency Translation	Cash Flow Hedges	Total
Balance, October 31, 2014	(4,551 )	991	(3,560 )
Other comprehensive income (loss) before reclassifications	(6,333 )	1,291	(5,042 )
Reclassifications	—	(784 )	(784 )
Balance, October 31, 2015	\$ (10,884 )	\$ 1,498	\$(9,386 )
Other comprehensive income (loss) before reclassifications	(1,441 )	1,431	(10 )
Reclassifications	—	(1,647 )	(1,647 )
Balance, October 31, 2016	\$ (12,325 )	\$ 1,282	\$(11,043 )

*Inventories.* Inventories are stated at the lower of cost or market, with cost determined using the first-in, first-out method. Provisions are made to reduce excess or obsolete inventories to their estimated realizable value.

*Property and Equipment.* Property and equipment are carried at cost. Depreciation and amortization of assets are provided primarily under the straight-line method over the shorter of the estimated useful lives or the lease terms as follows:

	Number of Years
Land	Indefinite
Building	40
Machines	7 – 10
Shop and office equipment	3 – 7
Leasehold improvements	3 – 40

Total depreciation and amortization expense recognized for property and equipment for the fiscal years ended October 31, 2016, 2015 and 2014 was \$2.5 million, \$2.2 million, and \$2.2 million, respectively.

**HURCO COMPANIES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued**

*Revenue Recognition.* We recognize revenue from sales of our machine tool systems upon delivery of the product to the customer, which is normally at the time of shipment, because persuasive evidence of an arrangement exists, delivery has occurred, the selling price is fixed and determinable and collectability is reasonably assured. Our computerized machine tools are general-purpose computer controlled machine tools that are typically used in stand-alone operations. Transfer of ownership and risk of loss are not contingent upon contractual customer acceptance. Prior to shipment, we test each machine to ensure the machine's compliance with standard operating specifications.

Depending upon geographic location, after shipment, a machine may be installed at the customer's facilities by a distributor, independent contractor or by one of our service technicians. In most instances where a machine is sold through a distributor, we have no installation involvement. If sales are direct or through sales agents, we will typically complete the machine installation, which consists of the reassembly of certain parts that were removed for shipping and the re-testing of the machine to ensure that it is performing within the standard specifications. We consider the machine installation process to be inconsequential and perfunctory.

Service fees from maintenance contracts are deferred and recognized in earnings on a pro rata basis over the term of the contract.

Sales related to software products are recognized when shipped in conformity with U.S. Generally Accepted Accounting Principles as promulgated by FASB guidance related to software revenue recognition that requires at the time of shipment, persuasive evidence of an arrangement exists, delivery has occurred, the selling price is fixed and determinable and collectability is reasonably assured. The software does not require production, modification or customization.

*Allowance for Doubtful Accounts.* The allowance for doubtful accounts is based on our best estimate of probable credit issues and historical experience. We perform credit evaluations of the financial condition of our customers. No collateral is required for sales made on open account terms. Concentrations of credit risk with respect to accounts receivable are limited due to the large number of customers comprising our customer base and their dispersion across many geographic areas. We consider trade accounts receivable to be past due when payment is not made by the due date as specified on the customer invoice, and charge off uncollectible balances when all reasonable collection efforts have been exhausted.

*Product Warranty.* Expected future product warranty claims are recorded to expense when the product is sold. Product warranty estimates are established using historical information about the nature, frequency, and average cost of warranty claims. Warranty claims are influenced by factors such as new product introductions, technological developments, the competitive environment, and the costs of component parts. Actual payments for warranty claims could differ from the amounts estimated requiring adjustments to the liabilities in future periods. See Note 12 of Notes to Consolidated Financial Statements for further discussion of warranties.

*Research and Development Costs.* The costs associated with research and development programs for new products and significant product improvements, other than software development costs which are eligible for capitalization per FASB guidance, are expensed as incurred and are included in Selling, general and administrative expenses. Research and development expenses totaled \$4.9 million, \$3.9 million, and \$3.4 million, in fiscal 2016, 2015, and 2014, respectively.

**HURCO COMPANIES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – Continued**

*Software Development Costs.* Costs incurred to develop computer software products and significant enhancements to software features of existing products to be sold or otherwise marketed are capitalized, after technological feasibility is established. Software development costs are amortized on a straight-line basis over the estimated product life of the related software, which ranges from three to five years. We capitalized costs of \$2.2 million in fiscal 2016, \$1.4 million in fiscal 2015, and \$1.0 million in fiscal 2014 related to software development projects. Amortization expense for software development costs was \$1.2 million, \$1.0 million, and \$1.2 million, for the fiscal years ended October 31, 2016, 2015, and 2014, respectively. Accumulated amortization at October 31, 2016 and 2015 was \$16.5 million and \$15.3 million, respectively. Estimated amortization expense for the remaining unamortized software development costs for the fiscal years ending October 31, is as follows (in thousands):

Fiscal Year	<b>Amortization Expense</b>
2017	\$ 1,200
2018	1,275
2019	750
2020	700
2021	625

*Goodwill and Intangible Assets.* Goodwill and other separately recognized intangible assets with indefinite lives are not subject to amortization. At least once annually or when indicators of impairment exist, we perform an impairment test for goodwill. Goodwill is allocated to various reporting units. We use a qualitative approach to test goodwill and indefinite-lived assets for impairment. Intangible assets that are determined to have a finite life are amortized over their estimated useful lives and are also subject to review for impairment, if indicators of impairment are identified. For fiscal years 2016 and 2015, using the qualitative approach to test for impairment, we concluded that goodwill and other intangible assets were not impaired.

As of October 31, 2016, the balances of intangible assets, other than goodwill, were as follows (in thousands):

Weighted Average Amortization Period	<b>Gross Intangible Assets</b>	<b>Accumulated Amortization</b>	<b>Net Intangible Assets</b>
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Tradenames and trademarks	13 years	\$ 231	\$ (59	)	\$ 172
Tradenames and trademarks	indefinite	60	—		60
Customer relationships	15 years	254	(114	)	140
Technology	13 years	672	(172	)	500
Patents	6 years	2,972	(2,741	)	231
Other	8 years	373	(326	)	47
Total		\$ 4,562	\$ (3,412	)	\$ 1,150

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**HURCO COMPANIES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – Continued**

As of October 31, 2015, the balances of intangible assets, other than goodwill, were as follows (in thousands):

	Weighted Average Amortization Period	Gross Intangible Assets	Accumulated Amortization	Net Intangible Assets
Tradenames and trademarks	13 years	\$ 231	\$ (41 )	\$ 190
Tradenames and trademarks	indefinite	60	—	60
Customer relationships	15 years	254	(97 )	157
Technology	13 years	674	(121 )	553
Patents	6 years	2,972	(2,717 )	255
Other	8 years	373	(299 )	74
Total		\$ 4,564	\$ (3,275 )	\$ 1,289

Intangible asset amortization expense was \$137,000, \$207,000, and \$412,000 for fiscal 2016, 2015 and 2014, respectively. Annual intangible asset amortization expense is estimated to be \$115,000 per year for fiscal years 2017 through 2021.

*Impairment of Long-Lived Assets.* We periodically evaluate the carrying value of long-lived assets to be held and used, including property and equipment, software development costs and intangible assets, including goodwill, when events or circumstances warrant such a review. The carrying value of a long-lived asset (or group of assets) to be held and used is considered impaired when the anticipated separately identifiable undiscounted cash flows from such an asset (or group of assets) are less than the carrying value of the asset (or group of assets) in accordance with FASB guidance related to accounting for the impairment or disposal of long-lived assets.

*Earnings Per Share.* Basic earnings per share is calculated by dividing net income by the weighted-average number of common shares actually outstanding during the period. Diluted earnings per share assumes the issuance of additional shares of common stock upon exercise of all outstanding stock options and contingently issuable securities if the effect is dilutive, in accordance with the treasury stock method discussed in FASB guidance on “Earnings Per Share”.

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The following table presents a reconciliation of our basic and diluted earnings per share computation:

(in thousands, except per share amounts)	Fiscal Year Ended October 31,					
	2016		2015		2014	
	Basic	Diluted	Basic	Diluted	Basic	Diluted
Net income	\$13,292	\$13,292	\$16,214	\$16,214	\$15,143	\$15,143
Undistributed earnings allocated to participating shares	(76 )	(76 )	(93 )	(93 )	(121 )	(121 )
Net income applicable to common shareholders	\$13,216	\$13,216	\$16,121	\$16,121	\$15,022	\$15,022
Weighted average shares outstanding	6,569	6,569	6,543	6,543	6,497	6,497
Stock options and contingently issuable securities	—	73	—	59	—	41
	6,569	6,642	6,543	6,602	6,497	6,538
Income per share	\$2.01	\$1.99	\$2.46	\$2.44	\$2.31	\$2.30

*Income Taxes.* We account for income taxes and the related accounts under the asset and liability method. Deferred tax assets and liabilities are measured using enacted income tax rates in each jurisdiction in effect for the year in which the temporary differences are expected to be recovered or settled. These deferred tax assets are reduced by a valuation allowance, which is established when it is more likely than not that some portion or all of the deferred tax assets will not be realized. Our judgment regarding the realization of deferred tax assets may change due to future profitability and market conditions, changes in U.S. or foreign tax laws and other factors. These changes, if any, may require material adjustments to these deferred tax assets and an accompanying reduction or increase in net income in the period when such determinations are made.

**HURCO COMPANIES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – Continued**

The determination of our provision for income taxes requires judgment, the use of estimates and the interpretation and application of complex tax laws. Our provision for income taxes reflects a combination of income earned and taxed at the federal and state level in the U.S., as well as in various foreign jurisdictions. We have not provided for any U.S. income taxes on the undistributed earnings of our foreign subsidiaries based upon our determination that such earnings will be indefinitely reinvested abroad. Undistributed earnings of our wholly-owned foreign subsidiaries at October 31, 2016 were approximately \$79.7 million. In the event these earnings are later distributed to the U.S., such distributions would likely result in additional U.S. tax that may be offset, at least in part, by associated foreign tax credits.

In addition to the risks to the effective tax rate described above, the future effective tax rate reflected in forward-looking statements is based on currently effective tax laws. Significant changes in those laws could materially affect these estimates.

We recognize uncertain tax positions when it is more likely than not that the tax position will be sustained upon examination by relevant taxing authorities, based on the technical merits of the position. The amount recognized is measured as the largest amount of benefit that is greater than 50 percent likely of being realized upon ultimate settlement.

*Stock Compensation.* We account for share-based compensation according to FASB guidance relating to share-based payments, which requires the measurement and recognition of compensation expense for all

share-based awards made to employees and directors based on estimated fair values on the grant date. This guidance requires that we estimate the fair value of share-based awards on the date of grant and recognize as expense the value of the portion of the award that is ultimately expected to vest over the requisite service period.

*Estimates.* The preparation of financial statements in conformity with U.S. Generally Accepted Accounting Principles requires us to make estimates and assumptions that affect the reported amounts presented and disclosed in our consolidated financial statements. Significant estimates and assumptions in these consolidated financial statements require the exercise of judgment and are used for, but not limited to, allowance for doubtful accounts, estimates of future cash flows and other assumptions associated with goodwill, intangible and long-lived asset impairment tests, useful lives for depreciation and amortization, warranty programs, stock compensation, income taxes and deferred tax valuation allowances, and contingencies. Due to the inherent uncertainty involved in making estimates, actual results reported in future periods may be different from these estimates.

## 2. BUSINESS OPERATIONS

*Nature of Business.* We design, manufacture and sell computerized CNC machine tools, computer control systems and software products, machine tool components, software options, control upgrades, accessories and replacement parts for our products, as well as customer service and training support, to companies in the metal cutting industry through a worldwide sales, service and distribution network. The machine tool industry is highly cyclical and changes in demand can occur abruptly in the geographic markets we serve. As a result of this cyclicity, we have experienced significant fluctuations in our sales, which, in periods of reduced demand, have adversely affected our results of operations and financial condition.

The end market for our products consists primarily of precision tool, die and mold manufacturers, independent job shops, and specialized short-run production applications within large manufacturing operations. Industries served include: aerospace, defense, medical equipment, energy, automotive/transportation, electronics and computer industries. Our products are sold through more than 195 independent agents and distributors throughout the Americas, Europe and Asia. We also have our own direct sales and service organizations in China, France, Germany, India, Italy, Poland, Singapore, South Africa, Taiwan, the United Kingdom, and certain areas of the United States.

**HURCO COMPANIES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – Continued**

*Credit Risk.* We sell products to customers located throughout the world. We perform ongoing credit evaluations of customers and generally do not require collateral. Allowances are maintained for potential credit losses. Concentration of credit risk with respect to trade accounts receivable is limited due to the large number of customers and their dispersion across many geographic areas. Although a significant amount of trade receivables are with distributors primarily located in the United States, no single distributor or region represents a significant concentration of credit risk.

*Manufacturing Risk.* At present, our wholly-owned subsidiaries, Hurco Manufacturing Limited (“HML”), Ningbo Hurco Manufacturing Limited (“NHML”) and Milltronics USA, Inc. (“Milltronics”) produce the vast majority of our machine tools for all three brands, Hurco, Milltronics and Takumi. In addition, we manufacture electro-mechanical components and accessories for machine tools through our wholly-owned subsidiary, LCM Precision Technology S.r.l. (“LCM”). HML, NHML, Milltronics and LCM manufacture their products in Taiwan, China, the U.S. and Italy, respectively. Any interruption in manufacturing at any of these locations would have an adverse effect on our financial operating results. Interruption in manufacturing at one of these locations could result from a change in the political environment or a natural disaster, such as an earthquake, typhoon, or tsunami. Any interruption with one of our key suppliers may also have an adverse effect on our operating results and our financial condition.

**3. INVENTORIES**

Inventories as of October 31, 2016 and 2015 are summarized below (in thousands):

	2016	2015
Purchased parts and sub-assemblies	\$25,661	\$25,914
Work-in-process	17,724	20,575
Finished goods	73,640	59,819
	\$117,025	\$106,308

Finished goods inventory consigned to our distributors and agents throughout the Americas, Europe and Asia was \$11.6 million and \$6.9 million as of October 31, 2016 and 2015, respectively.

**4. ACQUISITIONS OF BUSINESSES**

On July 14, 2015, we acquired the assets of the machine tool business of Milltronics Manufacturing Company, Inc., a U.S.-based manufacturer of CNC mills, lathes, and vertical and horizontal machining centers. We are operating this U.S. business as a product line through our wholly-owned subsidiary, Milltronics. Also, on July 28, 2015, we acquired the assets of the machine tool business of Takumi Machinery Co., Ltd. (“Takumi”), a Taiwan-based designer and manufacturer of CNC vertical machining centers, double column machining centers, high speed bridge machines and other machine tools equipped with industrial controls. We are operating this Taiwan business as a product line through our wholly-owned subsidiary, HML. These product lines contribute to our efforts to expand our consolidated product range, customer base and global platform, and accelerate emerging market penetration, particularly in strategic markets such as China and South America. The Hurco, Milltronics and Takumi product lines represent a comprehensive product portfolio with more than 150 different models. The combined machine tool product lines also provide benefits from the development of product enhancements, technologies and models due to leverage of shared resources and cross-utilization of proven engineering designs, allowing us to achieve manufacturing cost reductions from economies of scale and manufacturing efficiencies.

**HURCO COMPANIES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – Continued**

The acquisitions were accounted for in accordance with Accounting Standards Codification (“ASC”) Topic 805, Business Combinations. Accordingly, the total purchase price was initially allocated on a provisional basis to assets acquired and net liabilities assumed in connection with the acquisitions based on their estimated fair values as of the completion of the acquisitions. These allocations reflected various provisional estimates that were available at the time and were subject to change during the purchase price allocation period as valuations were finalized. All valuations are now final. The total fair value of the net assets acquired was approximately \$17.6 million, composed of \$12.5 million for Milltronics and \$5.1 million for Takumi. The results of operations of Milltronics and Takumi have been included in our consolidated financial statements from the respective dates of acquisition.

**5. CREDIT AGREEMENTS AND BORROWINGS**

On December 7, 2012, we entered into an agreement (the “U.S. credit agreement”) with a financial institution that provided us with a \$12.5 million unsecured revolving credit and letter of credit facility. The U.S. credit agreement permitted the issuance of up to \$3.0 million in letters of credit. On May 9, 2014, the maximum amount for outstanding letters of credit under our U.S. credit agreement was increased from \$3.0 million to \$5.0 million in order to guarantee a new revolving credit facility in Taiwan.

On June 5, 2014, we amended our U.S. credit agreement to increase the cash dividend allowance from \$1.0 million per calendar year to \$3.0 million per calendar year. On December 5, 2014, we amended our U.S. credit agreement to increase the cash dividend allowance from \$3.0 million per calendar year to \$4.0 million per calendar year and to extend the scheduled maturity date to December 7, 2016.

On December 6, 2016, we amended our U.S. credit agreement, among other things, to increase the unsecured revolving credit facility from \$12.5 million to \$15.0 million, to increase the cash dividend allowance from \$4.0 million per calendar year to \$5.0 million per calendar year, and to extend the scheduled maturity date to December 31, 2018. We also amended the U.S. credit agreement to increase the minimum working capital and minimum tangible net worth requirements from \$90.0 million to \$105.0 million and \$120.0 million to \$125.0 million, respectively.

Borrowings under the U.S. credit agreement bear interest either at a LIBOR-based rate or a floating rate, in each case with an interest rate floor of 0.00%. The floating rate equals the greatest of (a) a one month LIBOR-based rate plus 1.00% per annum, (b) the federal funds effective rate plus 0.50% per annum, (c) the prevailing prime rate, and (d) 0.00%. The rate we must pay for that portion of the U.S. credit agreement which is not utilized is 0.05% per annum.

The U.S. credit agreement contains customary financial covenants, including covenants (1) restricting us from making certain investments, loans, advances and acquisitions (but permitting us to make investments in subsidiaries of up to \$5.0 million), (2) requiring that we maintain a minimum working capital of \$105.0 million, and (3) requiring that we maintain a minimum tangible net worth of \$125.0 million. The U.S. credit agreement permits us to pay cash dividends in an amount not to exceed \$5.0 million per calendar year, so long as we are not in default before and after giving effect to such dividends.

We have a £1.0 million revolving credit facility in the United Kingdom and a €1.5 million revolving credit facility in Germany. On May 12, 2014, we established a Taiwan credit facility in the amount of 100.0 million New Taiwan Dollars with an expiration date of May 12, 2015. We did not renew this Taiwan credit facility. We also have a 40.0 million Chinese Yuan (approximately \$5.9 million) credit facility in China that was renewed on February 17, 2016 with an expiration date of February 16, 2017.

All of our credit facilities are unsecured.

At October 31, 2016, we had \$1.5 million of borrowings under our China credit facility which bears interest at 4.6% annually (variable rate). We had no other debt or borrowings under any of our other credit facilities.

**HURCO COMPANIES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – Continued**

At October 31, 2015, we had \$1.6 million of borrowings outstanding under our credit facility in China. At October 31, 2016, we were in compliance with all covenants contained in the related credit agreements and, as of that date, we had unutilized credit facilities of \$19.8 million.

**6. FINANCIAL INSTRUMENTS***Estimated Fair Value of Financial Instruments*

FASB fair value guidance establishes a three-tier fair value hierarchy, which categorizes the inputs used in measuring fair value. These tiers include: Level 1, defined as observable inputs, such as quoted prices in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs in which little or no market data exist, therefore requiring an entity to develop its own assumptions.

The carrying amounts for cash and cash equivalents approximate their fair values due to the short maturity of these instruments, and such instruments meet the Level 1 criteria of the three-tier fair value hierarchy discussed below. The carrying amount of short-term debt approximates fair value due to the variable rate of the interest and the short term nature of the instrument. The fair value of Level 2 is based on an internally developed model using current interest rate data for similar issues as there is no active market for this type of instrument.

In accordance with this guidance, the following table represents the fair value hierarchy for our financial assets and liabilities measured at fair value as of October 31, 2016 and 2015 (in thousands):

	Assets		Liabilities	
	October 31, 2016	October 31, 2015	October 31, 2016	October 31, 2015
Level 1				
Deferred compensation	\$ 1,363	\$ 1,310	\$-	\$ -

Level 2				
Derivatives	\$1,725	\$ 1,228	\$538	\$ 1,071

*Recurring Fair Value Measurements*

Included in Level 1 assets are mutual fund investments under a nonqualified deferred compensation plan. We estimate the fair value of these investments on a recurring basis using market prices which are readily available.

Included as Level 2 fair value measurements are derivative assets and liabilities related to gains and losses on foreign currency forward exchange contracts entered into with a third party. We estimate the fair value of these derivatives on a recurring basis using foreign currency exchange rates obtained from active markets. Derivative instruments are reported in the accompanying consolidated financial statements at fair value. We have derivative financial instruments in the form of foreign currency forward exchange contracts as described in Note 1 of Notes to Consolidated Financial Statements in which the U.S. Dollar equivalent notional amount of these contracts was \$125.6 million and \$109.6 million at October 31, 2016 and 2015, respectively. The fair value of Derivative assets recorded on our Consolidated Balance Sheets at October 31, 2016 and 2015 was \$1.7 million and \$1.2 million, respectively. The fair value of Derivative liabilities recorded on our Consolidated Balance Sheets at October 31, 2016 and 2015 was \$0.5 million and \$1.1 million, respectively.

The fair value of the foreign currency forward exchange contracts and the related currency positions are subject to offsetting market risk resulting from foreign currency exchange rate volatility. The counterparty to the forward exchange contract is a substantial and creditworthy financial institution. We do not consider either the risk of counterparty non-performance or the economic consequences of counterparty non-performance as material risks.

**HURCO COMPANIES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – Continued****7. INCOME TAXES**

In the fiscal years set forth below, the provision for income taxes consisted of the following (in thousands):

	Year Ended October 31,		
	2016	2015	2014
Current:			
U.S. taxes	\$1,362	\$4,600	\$3,498
Foreign taxes	4,456	3,752	3,594
	5,818	8,352	7,092
Deferred:			
U.S. taxes	(176 )	(896 )	(709 )
Foreign taxes	(49 )	(117 )	(165 )
	(225 )	(1,013 )	(874 )
	\$5,593	\$7,339	\$6,218

A comparison of income tax expense at the U.S. statutory rate to the Company's effective tax rate is as follows (dollars in thousands):

	Year Ended October 31,					
	2016		2015		2014	
Income before income taxes:						
Domestic	\$2,703		\$10,806		\$9,190	
Foreign	16,182		12,747		12,171	
Earnings (Loss) before taxes on income	\$18,885		\$23,553		\$21,361	
Tax rates:						
U.S. statutory rate	34	%	35	%	35	%
Effect of tax rate of international jurisdictions different than U.S. statutory rates	(7	)%	(5	)%	(4	)%
Valuation allowance	3	%	1	%	0	%
State taxes	0	%	1	%	0	%
Tax Credits	(2	)%	(1	)%	(1	)%
Effect of Tax Rate Changes	4	%	0	%	0	%
Other	(2	)%	0	%	(1	)%
Effective tax rate	30	%	31	%	29	%

We have not made any provision for U.S. income taxes on the undistributed earnings of our wholly-owned foreign subsidiaries based upon our determination that such earnings will be indefinitely reinvested. Undistributed earnings of our wholly-owned foreign subsidiaries at October 31, 2016 were approximately \$79.7 million. In the event these earnings are later distributed to the U.S., such distributions would likely result in additional U.S. tax that may be offset, at least in part, by associated foreign tax credits.

**HURCO COMPANIES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – Continued**

Deferred income taxes are determined based on the difference between the amounts used for financial reporting purposes and tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. Deferred taxes are adjusted for changes in tax rates and tax laws when changes are enacted. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realized.

As of October 31, 2016, we had deferred tax assets established for accumulated net operating loss carryforwards of \$1.6 million, primarily related to state and foreign jurisdictions. We also have deferred tax assets for research and development tax credits of \$0.5 million. We have established a valuation allowance against some of these carryforwards due to the uncertainty of their full realization. As of October 31, 2016 and 2015, the balance of this valuation allowance was \$2.1 million and \$1.5 million, respectively.

Significant components of our deferred tax assets and liabilities at October 31, 2016 and 2015 were as follows (in thousands):

	October 31,	
	2016	2015
<b>Deferred Tax Assets:</b>		
Accrued inventory reserves	1,824	1,304
Accrued warranty expenses	312	441
Compensation related expenses	2,664	1,891
Unrealized exchange gain/loss	370	186
Other accrued expenses	194	237
Net operating loss carryforwards	1,616	1,275
Other credit carryforwards	474	287
Other	331	170
	7,785	5,791
Less: Valuation allowance on net operating loss carryforwards	(1,593)	(1,300)
Valuation allowance on other credit carryforwards	(474 )	(185 )
	(2,067)	(1,485)
Deferred tax assets	5,718	4,306
<b>Deferred Tax Liabilities:</b>		
Net derivative instruments	(701 )	(811 )
Property and equipment and capitalized software development costs	(2,717)	(2,369)

Other	(456 )	(403 )
Net deferred tax assets	\$1,844	\$723

As of October 31, 2016, we had net operating losses carryforwards for international and U.S. income tax purposes of \$7.9 million, of which \$6.5 million will expire within 5 years and \$1.4 million will expire between 5 and 20 years. We also had tax credits of \$719,000 which will expire between 10 and 20 years.

A reconciliation of the beginning and ending amount of unrecognized tax benefits, excluding the related accrual for interest or penalties, is as follows (in thousands):

	2016	2015	2014
Balance, beginning of year	\$1,034	\$1,196	\$1,284
Additions based on tax positions related to the current year	52	17	5
Additions (reductions) related to prior year tax positions	19	(51 )	(4 )
Reductions due to statute expiration	—	—	—
Other	(3 )	(128 )	(89 )
Balance, end of year	\$1,102	\$1,034	\$1,196

**HURCO COMPANIES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – Continued**

The entire balance of the unrecognized tax benefits and related interest at October 31, 2016, if recognized, would favorably affect the effective tax rate in future periods.

We recognize accrued interest and penalties related to unrecognized tax benefits as components of our income tax provision. As of October 31, 2016, the gross amount of interest accrued, reported in other liabilities, was approximately \$53,000, which did not include the federal tax benefit of interest deductions. The statute of limitations with respect to unrecognized tax benefits will expire between July 2017 and July 2019.

Due to the uncertain and complex application of tax regulations, it is possible that the ultimate resolution of future audits may result in liabilities that could be different from this estimate. In such case, we would record additional tax expense or tax benefit in the tax provision (benefit) or reclassify amounts on the consolidated balance sheets in the period in which the matter is effectively settled with the taxing authority.

We file income tax returns in the U.S. federal jurisdiction and various states, local, and non-U.S. jurisdictions. There are currently no open audits in any jurisdictions.

A summary of open tax years by major jurisdiction is presented below:

United States federal	Fiscal 2013 through the current period
Germany <sup>1</sup>	Fiscal 2013 through the current period
Taiwan	Fiscal 2013 through the current period

<sup>1</sup> Includes federal as well as state, provincial or similar local jurisdictions, as applicable.

**8.EMPLOYEE BENEFITS**

We have defined contribution plans that include a majority of our employees, under which our matching contributions are primarily discretionary. The purpose of these plans is generally to provide additional financial security during retirement by providing employees with an incentive to save throughout their employment. Our contributions and related expense totaled \$1.1 million, \$933,000, and \$884,000, for the fiscal years ended October 31, 2016, 2015 and 2014, respectively.

## **9. STOCK-BASED COMPENSATION**

In March 2016, we adopted the Hurco Companies, Inc. 2016 Equity Incentive Plan (the “2016 Equity Plan”), which allows us to grant awards of stock options, stock appreciation rights (“SARs”), restricted stock, stock units and other stock-based awards. The 2016 Equity Plan replaced the 2008 Equity Incentive Plan (the “2008 Plan”) and is the only active plan under which equity awards may be made to our employees and non-employee directors. No further awards will be made under our 2008 Plan. The total number of shares of our common stock that may be issued pursuant to awards under the 2016 Equity Plan is 856,048, which included 386,048 shares remaining available for future grants under the 2008 Plan as of March 10, 2016, the date of shareholder approval of the 2016 Equity Plan.

The Compensation Committee of the Board of Directors has the authority to determine the officers, directors and key employees who will be granted awards; designate the number of shares subject to each award; determine the terms and conditions upon which awards will be granted; and prescribe the form and terms of award agreements. We have granted restricted shares under the 2016 Equity Plan which are currently outstanding, and we have granted stock options, restricted shares and performance shares under the 2008 Plan which are currently outstanding. No stock option may be exercised more than ten years after the date of grant or such shorter period as the Compensation Committee may determine at the date of grant. The market value of a share of our common stock, for purposes of the 2016 Equity Plan, is the closing sale price as reported by the Nasdaq Global Select Market on the date in question or, if not a trading day, on the last preceding trading date.

**HURCO COMPANIES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – Continued**

During fiscal 2016, we recorded approximately \$1.6 million of stock-based compensation expense related to grants under the 2008 Plan and the 2016 Equity Plan. We recorded approximately \$1.2 million and \$921,000 of stock-based compensation expense related to grants under the 2008 Plan for fiscal 2015 and 2014, respectively. As of October 31, 2016, there was an estimated \$2.0 million of total unrecognized stock-based compensation cost that we expect to recognize by the end of the first quarter of fiscal 2019.

On March 10, 2016, the Compensation Committee granted a total of 9,170 shares of time-based restricted stock to our non-employee directors under the 2016 Equity Plan. The restricted shares vest in full one year from the date of grant provided the recipient remains on the board of directors through that date. The grant date fair value of the restricted shares was based on the closing sales price of our common stock on the grant date which was \$30.52 per share.

On January 4, 2016, the Compensation Committee approved a long-term incentive compensation arrangement for our executive officers in the form of restricted shares and performance shares awarded under the 2008 Plan. The awards were 25% time-based vesting and 75% performance-based vesting. The three-year performance period is fiscal 2016 through fiscal 2018.

On that date, the Compensation Committee granted a total of 17,684 shares of time-based restricted shares to our executive officers. The restricted shares vest in thirds over three years from the date of grant provided the recipient remains employed through that date. The grant date fair value of the restricted shares was based upon the closing sales price of our common stock on the date of grant which was \$26.04 per share.

On January 4, 2016, the Compensation Committee also granted a total target number of 24,023 performance shares to our executive officers designated as “Performance Shares – TSR”. The shares were weighted as 40% of the overall long-term incentive compensation arrangement and will vest and be paid based upon our total shareholder return of our common stock over a three-year period, relative to the total shareholder return of the companies in a specified peer group over that period. Participants will have the ability to earn between 50% of the target number of shares for achieving threshold performance and 200% of the target number of shares for achieving maximum performance. The fair value of the market-based performance shares was \$30.67 per share and was calculated using the Monte Carlo approach.

On January 4, 2016, the Compensation Committee also granted a total target number of 24,759 performance shares to our executive officers designated as “Performance Shares – ROIC”. These shares were weighted as 35% of the overall long-term incentive compensation arrangement and will vest and be paid based upon the achievement of pre-established goals related to our average return on invested capital over the three-year period. Participants will have the ability to earn between 50% of the target number of shares for achieving threshold performance and 200% of the target number of shares for achieving maximum performance. The grant date fair value of the ROIC performance shares was based on the closing sales price of our common stock on the grant date which was \$26.04 per share.

On March 12, 2015, the Compensation Committee granted a total of 9,086 shares of restricted stock to our non-employee directors. The restricted stock vests in full one year from the date of grant provided the recipient remains on the board of directors through that date. The grant date fair value of restricted stock was based on the closing sales price of our common stock on the grant date which was \$30.80 per share.

On January 6, 2015, the Compensation Committee approved a long-term incentive compensation arrangement for our executive officers in the form of restricted shares and performance shares awarded under the 2008 Plan. The awards were 25% time-based vesting and 75% performance-based vesting. The three-year performance period is fiscal 2015 through fiscal 2017.

**HURCO COMPANIES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – Continued**

On that date, the Compensation Committee granted a total of 11,174 shares of time-based restricted shares to our executive officers. The restricted shares vest in thirds over three years from the date of grant provided the recipient remains employed through that date. The grant date fair value of the restricted shares was based upon the closing sales price of our common stock on the date of grant which was \$32.22.

On January 6, 2015, the Compensation Committee also granted a total target number of 16,740 performance shares to our executive officers designated as “Performance Shares – TSR”. The shares were weighted as 40% of the overall long-term incentive compensation arrangement and will vest and be paid based upon our total shareholder return of our common stock over a three-year period, relative to the total shareholder return of the companies in a specified peer group over that period. Participants will have the ability to earn between 50% of the target number of shares for achieving threshold performance and 200% of the target number of shares for achieving maximum performance. The fair value of the market-based performance shares was \$34.41 per share and was calculated using the Monte Carlo approach.

On January 6, 2015, the Compensation Committee also granted a total target number of 15,643 performance shares to our executive officers designated as “Performance Shares – ROIC”. These shares were weighted as 35% of the overall long-term incentive compensation arrangement and will vest and be paid based upon the achievement of pre-established goals related to our average return on invested capital over the three-year period. Participants will have the ability to earn between 50% of the target number of shares for achieving threshold performance and 200% of the target number of shares for achieving maximum performance. The grant date fair value of the ROIC performance shares was based on the closing sales price of our common stock on the grant date which was \$32.22 per share.

On March 13, 2014, the Compensation Committee granted a total of 11,235 shares of restricted stock to our non-employee directors. The restricted stock vests in full one year from the date of grant provided the recipient remains on the board of directors through that date. The grant date fair value of the restricted stock was based on the closing sales price of our common stock on the grant date which was \$24.92 per share.

On January 10, 2014, the Compensation Committee approved a long-term incentive compensation arrangement for our executive officers in the form of restricted shares and performance shares awarded under the 2008 Plan. The awards were 25% time-based vesting and 75% performance-based vesting. The three-year performance period is fiscal 2014 through fiscal 2016.

On that date, the Compensation Committee granted a total 12,182 shares of time-based restricted shares to our executive officers. The restricted shares vest in thirds over three years from the date of grant provided the recipient remains employed through that date. The grant date fair value of the restricted shares was based upon the closing sales price of our common stock on the date of grant which was \$24.01 per share.

On January 10, 2014, the Compensation Committee also granted a total target number of 16,948 performance shares to our executive officers designated as “Performance Shares –TSR”. The shares were weighted as 40% of the overall long-term incentive compensation arrangement and will vest and be paid based upon the total shareholder return of our common stock over a three-year period, relative to the total shareholder return of the companies in a specified peer group over that period. Participants will have the ability to earn between 50% of the target number of shares for achieving threshold performance and 200% of the target number of shares for achieving maximum performance. The fair value of the market-based performance shares was \$26.43 per share and was calculated using the Monte Carlo approach.

**HURCO COMPANIES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – Continued**

On January 10, 2014, the Compensation Committee also granted a total target number of 17,056 performance shares to our executive officers designated as “Performance Shares –ROIC”. These shares were weighted as 35% of the overall long-term incentive compensation arrangement and will vest and be paid based upon the achievement of pre-established goals related to our average return on invested capital over the three-year period. Participants will have the ability to earn between 50% of the target number of shares for achieving threshold performance and 200% of the target number of shares for achieving maximum performance. The grant date fair value of the ROIC performance shares was based on the closing sales price of our common stock on the grant date which was \$24.01 per share.

A reconciliation of the Company’s restricted stock activity and related information is as follows:

	Number of Shares	Weighted Average Grant Date Fair Value
Unvested at October 31, 2015	98,799	\$ 28.89
Shares granted	75,636	28.05
Shares vested	(21,385 )	27.63
Shares withheld	(5,700 )	25.29
Unvested at October 31, 2016	147,350	\$ 28.79

A summary of the status of the options as of October 31, 2016, 2015 and 2014 and the related activity for the year is as follows:

	<b>Shares Under Option</b>	Weighted Average Exercise Price Per Share
Balance October 31, 2013	168,712	\$ 20.73
Granted	—	—
Cancelled	(20,217 )	25.59
Expired	—	—
Exercised	(20,306 )	17.67
Balance October 31, 2014	128,189	\$ 20.45
Granted	—	—

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Cancelled	(5,000	)	35.83
Expired	—		—
Exercised	(15,300	)	16.81
Balance October 31, 2015	107,889		\$ 20.25
Granted	—		—
Cancelled	—		—
Expired	—		—
Exercised	—		—
Balance October 31, 2016	107,889		\$ 20.25

The total intrinsic value of stock options exercised during the twelve months ended October 31, 2016, 2015 and 2014 was approximately \$0, \$154,000 and \$424,000, respectively.

**HURCO COMPANIES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – Continued**

As of October 31, 2016, the total intrinsic value of outstanding stock options already vested and expected to vest and the intrinsic value of options that are outstanding and exercisable was \$690,000. Stock options outstanding and exercisable on October 31, 2016, are as follows:

Range of Exercise Prices Per Share	Shares Under Option	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Life in Years
<b>Outstanding</b>			
\$ 14.82	24,000	\$ 14.82	3.1
14.88	4,200	14.88	2.5
18.13	16,000	18.13	3.5
21.45	37,841	21.45	5.1
23.30	20,848	23.30	6.1
35.83	5,000	35.83	1.6
\$ 14.82 – 35.83	107,889	\$ 20.25	4.4
<b>Exercisable</b>			
\$ 14.82	24,000	\$ 14.82	3.1
14.88	4,200	14.88	2.5
18.13	16,000	18.13	3.5
21.45	37,841	21.45	5.1
23.30	20,848	23.30	6.1
35.83	5,000	35.83	1.6
\$ 14.82 – 35.83	107,889	\$ 20.25	4.4

**10. RELATED PARTY TRANSACTIONS**

As of October 31, 2016, we owned approximately 35% of the outstanding shares of a Taiwanese-based contract manufacturer, Hurco Automation, Ltd. (“HAL”). HAL’s scope of activities includes the design, manufacture, sales and distribution of industrial automation products, software systems and related components, including control systems and components produced under contract for sale exclusively to us. We are accounting for this investment using the equity method. The investment of \$3.6 million and \$3.0 million at October 31, 2016 and 2015, respectively, is included in Investments and other assets, net on the Consolidated Balance Sheets. Purchases of controls from HAL amounted to \$9.9 million, \$8.9 million and \$9.3 million in fiscal 2016, 2015 and 2014, respectively. Sales of control component parts to HAL were \$623,000, \$723,000 and \$1.4 million for the fiscal years ended October 31, 2016, 2015 and 2014, respectively. Trade payables to HAL were \$2.0 million and \$1.8 million at October 31, 2016 and 2015,

respectively. Trade receivables from HAL were \$94,000 and \$55,000 at October 31, 2016 and 2015, respectively.

Summary unaudited financial information for HAL's operations and financial condition is as follows (in thousands):

	2016	2015	2014
Net Sales	\$13,948	\$12,852	\$12,063
Gross Profit	2,240	2,041	1,759
Operating Income	952	665	468
Net Income	1,323	1,546	1,264
Current Assets	\$10,238	\$10,262	\$10,469
Non-current Assets	3,733	3,087	3,065
Current Liabilities	2,572	3,472	3,637

**HURCO COMPANIES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – Continued****11. CONTINGENCIES AND LITIGATION**

We are involved in various claims and lawsuits arising in the normal course of business. Pursuant to applicable accounting rules, we accrue the minimum liability for each known claim when the estimated outcome is a range of possible loss and no one amount within that range is more likely than another. We maintain insurance policies for such matters, and we record insurance recoveries when we determine such recovery to be probable. We do not expect any of these claims, individually or in the aggregate, to have a material adverse effect on our consolidated financial position or results of operations. We believe that the ultimate resolution of claims for any losses will not exceed our insurance policy coverages.

**12. GUARANTEES AND PRODUCT WARRANTIES**

From time to time, our subsidiaries guarantee third party payment obligations in connection with the sale of machines to customers that use financing. We follow FASB guidance for accounting for guarantees (codified in ASC 460). As of October 31, 2016, we had 26 outstanding third party payment guarantees totaling approximately \$1.2 million. The terms of these guarantees are consistent with the underlying customer financing terms. Upon shipment of a machine, the customer has the risk of ownership. The customer does not obtain title, however, until it has paid for the machine. A retention of title clause allows us to recover the machine if the customer defaults on the financing. We accrue liabilities under these guarantees at fair value, which amounts are insignificant.

We provide warranties on our products with respect to defects in material and workmanship. The terms of these warranties are generally one year for machines and shorter periods for service parts. We recognize a reserve with respect to this obligation at the time of product sale, with subsequent warranty claims recorded against the reserve. The amount of the warranty reserve is determined based on historical trend experience and any known warranty issues that could cause future warranty costs to differ from historical experience. A reconciliation of the changes in our warranty reserve is as follows (in thousands):

	2016	2015	2014
Balance, beginning of year	\$2,186	\$2,048	\$1,778
Provision for warranties during the year	2,715	3,736	3,846
Charges to the accrual	(3,349)	(3,495)	(3,529)
Impact of foreign currency translation	(29 )	(103 )	(47 )
Balance, end of year	\$1,523	\$2,186	\$2,048

The decrease in our warranty reserve in fiscal 2016 compared to 2015 was primarily due to a reduction in unit sales volume, as well as a reduction in average warranty cost per machine as our product mix of machines under warranty shifted from more complex, higher-performance machines. The fiscal 2016 reduction in warranty reserve was also attributable to reductions in warranty obligations assumed as part of the acquisition of Milltronics and Takumi, as actual claims were less than anticipated, resulting in adjustments to the provision for warranties during the year. The increase in warranty reserve from fiscal 2014 to 2015 included \$241,000 of warranty obligations assumed as part of the acquisitions of Milltronics and Takumi.

**HURCO COMPANIES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued****13. OPERATING LEASES**

We lease facilities, certain equipment and vehicles under operating leases that expire at various dates through 2024. Future payments required under operating leases as of October 31, 2016, are summarized as follows (in thousands):

2017	\$2,929
2018	1,573
2019	911
2020	377
2021 and thereafter	556
Total	\$6,346

Lease expense for the fiscal years ended October 31, 2016, 2015, and 2014 was \$4.5 million, \$3.8 million, and \$4.0 million, respectively.

**14. QUARTERLY FINANCIAL INFORMATION (Unaudited)**

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
2016 (In thousands, except per share data)				
Sales and service fees	\$56,503	\$52,029	\$52,403	\$66,354
Gross profit	17,698	16,610	16,135	19,997
Gross profit margin	31 %	32 %	31 %	30 %
Selling, general and administrative expenses	11,961	11,943	12,042	14,878
Operating income	5,737	4,667	4,093	5,119
Provision for income taxes	1,709	1,225	1,120	1,539
Net income	3,895	3,674	2,720	3,003
Income per common share – basic	\$0.59	\$0.56	\$0.41	\$0.45
Income per common share – diluted	\$0.58	\$0.56	\$0.40	\$0.45

	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
2015 (In thousands, except per share data)				

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Sales and service fees	\$50,972	\$50,183	\$52,535	\$65,693
Gross profit	16,547	16,559	16,630	19,355
Gross profit margin	32 %	33 %	32 %	29 %
Selling, general and administrative expenses	10,454	10,850	11,351	12,632
Operating income	6,093	5,709	5,279	6,723
Provision for income taxes	2,037	1,878	1,573	1,851
Net income	3,766	3,961	3,683	4,804
Income per common share – basic	\$0.57	\$0.60	\$0.56	\$0.73
Income per common share – diluted	\$0.57	\$0.60	\$0.55	\$0.72

**HURCO COMPANIES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued****15. SEGMENT INFORMATION**

We operate in a single segment: industrial automation equipment. We design, manufacture and sell computerized (i.e., Computer Numeric Control) machine tools, consisting primarily of vertical machining centers (mills) and turning centers (lathes), to companies in the metal cutting industry through a worldwide sales, service and distribution network. Although the majority of our computer control systems and software products are proprietary, they predominantly use industry standard personal computer components. Our computer control systems and software products are primarily sold as integral components of our computerized machine tool products. We also provide machine tool components, software options, control upgrades, accessories and replacement parts for our products, as well as customer service and training support.

We sell our products through more than 195 independent agents and distributors throughout the Americas, Europe and Asia. Our line is the primary line for the majority of our distributors globally even though some may carry competitive products. We also have our own direct sales and service organizations in China, France, Germany, India, Italy, Poland, Singapore, South Africa, Taiwan, the United Kingdom, and certain areas of the United States, which are among the world's principal machine tool consuming countries. During fiscal 2016, no distributor accounted for more than 5% of our sales and service fees. In fiscal 2016, approximately 69% of our revenues were from customers located outside of the U.S. and no single end-user of our products accounted for more than 5% of our total sales and service fees.

The following table sets forth the contribution of each of our product groups to our total sales and service fees during each of the past three fiscal years (in thousands):

**Net Sales and Service Fees by Product Category**

	Year ended October 31,		
	2016	2015	2014
Computerized Machine Tools *	\$195,618	\$189,712	\$193,937
Computer Control Systems and Software †	2,078	3,085	3,407
Service Parts	21,908	19,375	17,391
Service Fees	7,685	7,211	7,568

Total	\$227,289	\$219,383	\$222,303
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\* Amounts shown include sales of Milltronics and Takumi computerized machine tools to third parties since the respective dates of acquisitions.

†Amounts shown do not include computer control systems and software sold as an integrated component of computerized machine systems.

**HURCO COMPANIES, INC.****NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued**

The following table sets forth revenues by geographic area, based on customer location, for each of the past three fiscal years (in thousands):

**Revenues by Geographic Area**

	Year Ended October 31,		
	2016	2015	2014
United States of America	\$70,630	\$66,781	\$59,414
Canada	3,881	3,114	2,434
South America	1,950	1,930	450
Total Americas	76,461	71,825	62,298
Germany	44,411	43,727	51,581
United Kingdom	25,313	30,235	34,288
Italy	12,947	11,768	13,456
France	13,787	13,162	9,972
Other Europe	27,150	26,598	24,728
Total Europe	123,608	125,490	134,025
Asia Pacific	25,633	20,265	23,766
Other Foreign	1,587	1,803	2,214
Total Europe, Asia Pacific and Other Foreign	150,828	147,558	160,005
	\$227,289	\$219,383	\$222,303

Long-lived tangible assets, net by geographic area, were (in thousands):

	As of October 31,	
	2016	2015
United States of America	\$7,846	\$8,658
Foreign countries	5,911	5,893
	\$13,757	\$14,551

Net assets by geographic area were (in thousands):

	As of October 31,	
	2016	2015
Americas	\$84,040	\$83,236
Europe	60,861	59,468
Asia Pacific	40,574	31,864
	\$185,475	\$174,568

## 16. NEW ACCOUNTING PRONOUNCEMENTS

### Recently Adopted Accounting Pronouncement:

In November 2015, the FASB issued Accounting Standards Update (“ASU”) No. 2015-17, *Balance Sheet Classification of Deferred Taxes*, which requires companies to present deferred income tax assets and deferred income tax liabilities as noncurrent in a classified balance sheet instead of the current requirement to separate deferred income tax liabilities and assets into current and noncurrent amounts. ASU 2015-17 is effective for fiscal years beginning after December 15, 2016, including interim periods within those fiscal years. Early application is permitted either prospectively or retrospectively. We adopted this accounting update in the first quarter of fiscal 2016 and applied it retrospectively to prior periods. The impact on our October 31, 2015 Consolidated Balance Sheet was a reduction in Total current assets of \$2.0 million, an increase in Total non-current assets of \$4.7 million, and an increase in Total non-current liabilities of \$2.7 million.

**HURCO COMPANIES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued**

*New Accounting Pronouncements:*

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, establishing a single comprehensive model for entities to use in accounting for revenue arising from contracts with customers. This update provides a five-step analysis in determining when and how revenue is recognized. The new model will require revenue recognition to depict the transfer of promised goods or services to customers in an amount that reflects the consideration a company expects to receive in exchange for those goods or services and will supersede most of the existing revenue recognition guidance, including industry-specific guidance. We have the option of using either a full retrospective or modified approach to adopt this guidance. Between August 2015 and May 2016, the FASB issued four additional updates to Topic 606: 1) ASU No. 2015-14, *Deferral of the Effective Date*, 2) ASU No. 2016-08, *Principal versus Agent Considerations (Reporting Revenue Gross versus Net)*, 3) ASU No. 2016-10, *Identifying Performance Obligations and Licensing*, and 4) ASU No. 2016-12, *Narrow-Scope Improvements and Practical Expedients* to provide further guidance and clarification in accounting for revenue arising from contracts with customers. All these updates will be effective for our fiscal year 2019, including interim periods within the fiscal year. We are assessing the method of adoption and the impact this new accounting guidance will have on our consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15, *Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern*, which requires management to evaluate whether there is substantial doubt about an entity's ability to continue as a going concern and provide related footnote disclosures. ASU No. 2014-15 is effective for our fiscal year 2018, including interim periods within the fiscal year. Early adoption is permitted for financial statements that have not been previously issued. We do not expect that the adoption of this accounting standard update will have a material effect on our consolidated financial statements.

In January 2016, the FASB issued ASU No. 2016-01 *Financial Instruments - Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities*, which amends the guidance on the classification and measurement of financial instruments under the fair value option, as well as the presentation and disclosure requirements for financial instruments. Among other things, ASU No. 2016-01 requires equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income. In addition, ASU No. 2016-01 requires public companies to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes, to separate presentation of financial assets and financial liabilities by measurement category and form of financial asset, and to eliminate the requirement to disclose the method(s) and significant assumptions used to estimate the fair value of financial instruments measured at amortized cost. ASU No. 2016-01 is effective for our fiscal year 2019, including interim periods within the fiscal year. We are assessing the impact this new accounting guidance will have on our consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, *Leases (Topic 842)*, which establishes a comprehensive new lease accounting model. ASU 2016-02 clarifies the definition of a lease, requires a dual approach to lease classification similar to current lease classifications, and requires lessees to recognize leases on the balance sheet as a lease liability with a corresponding right-of-use asset for leases with a lease-term of more than twelve months. ASU 2016-02 is effective for our fiscal year 2020, including interim periods within the fiscal year, and requires modified retrospective application. Early adoption is permitted. We are assessing the impact this new accounting guidance will have on our consolidated financial statements.

In March 2016, the FASB issued ASU No. 2016-09, *Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*, which simplifies several areas of accounting for share-based compensation arrangements, including income tax consequences, classification of awards as either equity or liabilities, and classification on the statement of cash flows. ASU 2016-09 is effective for our fiscal year 2018, including interim periods within the fiscal year. Early adoption is permitted. We are assessing the impact this new accounting guidance will have on our consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, *Statement of Cash Flows (Topic 230) - a Consensus of the FASB's Emerging Issues Task Force*, which provides guidance intended to reduce diversity in practice in how certain transactions are classified in the statement of cash flows. ASU 2016-15 is effective for our fiscal year 2018. We do not expect that the adoption of this accounting standard update will have a material effect on our consolidated financial statements.

**HURCO COMPANIES, INC.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued**

In October 2016, the FASB issued ASU No. 2016-16, *Accounting for Income Taxes: Intra-Entity Asset Transfers of Assets Other than Inventory*, which removes the prohibition in ASC 740 (Income Taxes) against the immediate recognition of the current and deferred income tax effects of intra-entity transfers of assets other than inventory. ASU 2016-16 is effective for our fiscal year 2019, including interim periods within those fiscal years. Early adoption is permitted however the guidance can only be adopted in the first interim period of a fiscal year. We are assessing the impact this new accounting guidance will have on our consolidated financial statements.

There have been no other significant changes in the Company's critical accounting policies and estimates during the fiscal year ended October 31, 2016.

**Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure**

None.

**Item 9A. CONTROLS AND PROCEDURES**

Under the supervision and with the participation of management, including our Chief Executive Officer and Chief Financial Officer, we carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures as of October 31, 2016, pursuant to Rule 13a-15(b) under the Securities Exchange Act of 1934, as amended. Based upon that evaluation, our management, including the Chief Executive Officer and Chief Financial Officer, concluded that our disclosure controls and procedures were effective as of the evaluation date.

There have been no changes in our internal control over financial reporting that occurred during the fourth quarter of the fiscal year ended October 31, 2016 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

The attestation report of our independent registered public accounting firm on our internal control over financial reporting is included in this report under Item 8. Financial Statements and Supplementary Data. Our management's annual report on internal control over financial reporting is included in this report immediately preceding Item 8.

**Item 9B. OTHER INFORMATION**

During the fourth quarter of fiscal 2016, the Audit Committee of the Board of Directors did not engage our independent registered public accounting firm to perform any new non-audit services. This disclosure is made pursuant to Section 10A(i)(2) of the Securities Exchange Act of 1934, as added by Section 202 of the Sarbanes-Oxley Act of 2002.

The graph below compares the 5-Year cumulative total return on our common stock relative to that of the Russell 2000 Index and two customized peer groups of twenty companies and nineteen companies respectively, whose individual companies are listed below. An investment of \$100 (with reinvestment of all dividends) is assumed to have been made in our common stock, in each Index and in each of the peer groups on 10/31/2011 and its relative performance is tracked through 10/31/2016.

	<b>10/11</b>	<b>10/12</b>	<b>10/13</b>	<b>10/14</b>	<b>10/15</b>	<b>10/16</b>
Hurco Companies, Inc.	100.00	87.98	94.11	149.40	105.20	103.84
Russell 2000	100.00	112.08	152.75	165.07	165.62	172.43
2015 Peer Group	100.00	96.96	151.68	145.28	121.96	132.35
2016 Peer Group	100.00	97.07	150.82	141.32	120.93	129.77

*The stock price performance included in this graph is not necessarily indicative of future stock price performance.*

**2015 Peer Group:** The twenty companies included in the company's 2015 peer group are: Ampco-Pittsburgh Corporation, Douglas Dynamics, Inc., Dynamic Materials Corporation, The Eastern Company, Electro Scientific Industries, Inc., FARO Technologies Inc., Graham Corporation, Hardinge Inc., Kadant Inc., Key Technology, Inc., Key Tronic Corporation, The L.S. Starrett Company, Nanometrics Incorporated, NN Inc., Novanta Inc. (formerly GSI Group, Inc.), PDF Solutions, Inc., Proto Labs, Inc., QAD Inc., Sun Hydraulics Corp. and Transcat Inc.

**2016 Peer Group:** The nineteen companies included in the company's 2016 peer group are: Ampco-Pittsburgh Corporation, Douglas Dynamics, Inc., Dynamic Materials Corporation, The Eastern Company, Electro Scientific Industries, Inc., FARO Technologies Inc., Graham Corporation, Hardinge Inc., Kadant Inc., Key Technology, Inc., Key Tronic Corporation, The L.S. Starrett Company, Nanometrics Incorporated, Novanta Inc., PDF Solutions, Inc., Proto Labs, Inc., QAD Inc., Sun Hydraulics Corp. and Transcat Inc.



## **PART III**

### **Item 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE**

The information required by this item is incorporated herein by reference to the definitive proxy statement for our 2017 annual meeting of shareholders except that the information required by Item 10 regarding our executive officers is included herein under a separate caption at the end of Part I.

### **Item 11. EXECUTIVE COMPENSATION**

The information required by this item is incorporated herein by reference to the definitive proxy statement for our 2017 annual meeting of shareholders.

### **Item 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS**

The information required by this item is incorporated herein by reference to the definitive proxy statement for our 2017 annual meeting of shareholders.

### **Item 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS, AND DIRECTOR INDEPENDENCE**

The information required by this item is incorporated herein by reference to the definitive proxy statement for our 2017 annual meeting of shareholders.

### **Item 14. PRINCIPAL ACCOUNTING FEES AND SERVICES**

The information required by this item is incorporated herein by reference to the definitive proxy statement for our 2017 annual meeting of shareholders.



**PART IV**

**Item 15. Exhibits AND Financial Statement Schedules**

(a) 1. Financial Statements. The following consolidated financial statements of the Company are included herein under Item 8 of Part II:

	Page
Reports of Independent Registered Public Accounting Firm	35
Consolidated Statements of Income – years ended October 31, 2016, 2015 and 2014	37
Consolidated Statements of Comprehensive Income – years ended October 31, 2016, 2015 and 2014	38
Consolidated Balance Sheets – as of October 31, 2016 and 2015	39
Consolidated Statements of Cash Flows – years ended October 31, 2016, 2015 and 2014	40
Consolidated Statements of Changes in Shareholders’ Equity – years ended October 31, 2016, 2015 and 2014	41
Notes to Consolidated Financial Statements	42

2. Financial Statement Schedule. The following financial statement schedule is included in this Item.

	Page
Schedule II - Valuation and Qualifying Accounts and Reserves	70

All other financial statement schedules are omitted because they are not applicable or the required information is included in the consolidated financial statements or notes thereto.

(b)

Exhibits

Exhibits being filed with this Form 10-K or incorporated herein by reference are listed on page 71.

**Schedule II - Valuation and Qualifying Accounts and Reserves****for the Years Ended October 31, 2016, 2015, and 2014**

(Dollars in thousands)

Description	Balance at Beginning of Period	Charged to/ (Recovered from) Costs and Expenses	Charged to Other Accounts	Deductions	Balance at End of Period
Allowance for doubtful accounts for the year ended:					
October 31, 2016	\$ 739	\$ (15 )	\$ —	\$ 60	(1) \$ 664
October 31, 2015	\$ 878	\$ (13 )	\$ —	\$ 126	(1) \$ 739
October 31, 2014	\$ 540	\$ 446	\$ —	\$ 108	(1) \$ 878
Income tax valuation allowance for the year ended:					
October 31, 2016	\$ 1,485	\$ 587	\$ —	\$ 5	\$ 2,067
October 31, 2015	\$ 1,225	\$ 402	\$ —	\$ 142	\$ 1,485
October 31, 2014	\$ 1,199	\$ 81	\$ —	\$ 55	\$ 1,225

<sup>(1)</sup> Receivable write-offs.

## EXHIBITS INDEX

Exhibits Filed. The following exhibits are filed with this report:

- 21 Subsidiaries of the Registrant.
- 23 Consent of Independent Registered Public Accounting Firm, Ernst & Young LLP
- 31.1 Certification by the Chief Executive Officer, pursuant to Rule 13a-14(a) under the Securities and Exchange Act of 1934, as amended.
- 31.2 Certification by the Chief Financial Officer, pursuant to Rule 13a-14(a) under the Securities and Exchange Act of 1934, as amended.
- 32.1 Certification by the Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 32.2 Certification by the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101.INSXBRL Instance Document\*