

UFP TECHNOLOGIES INC  
Form 10-Q  
May 10, 2013  
Table of Contents

# UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

## FORM 10-Q

(Mark one)

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

For the quarterly period ended MARCH 31, 2013

OR

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

For the transition period from        to

Commission File Number: 001-12648

**UFP Technologies, Inc.**

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(Exact name of registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of incorporation or organization)

**04-2314970**

(IRS Employer Identification No.)

**172 East Main Street, Georgetown, Massachusetts 01833, USA**

(Address of principal executive offices) (Zip Code)

**(978) 352-2200**

(Registrant's telephone number, including area code)

(Former name, former address, and former fiscal year, if changed since last report)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ; No

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

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

[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

6,796,959 shares of registrant's Common Stock, \$.01 par value, were outstanding as of May 2, 2013.



Table of Contents

**UFP Technologies, Inc.**

**Index**

|  | <b>Page</b> |
|--|-------------|
| <b><u>PART I - FINANCIAL INFORMATION</u></b>   | 3           |
| <b><u>Item 1. Financial Statements</u></b>   | 3           |
| <u>Condensed Consolidated Balance Sheets as of March 31, 2013 (unaudited) and December 31, 2012</u>                              | 3           |
| <u>Condensed Consolidated Statements of Income for the Three Months Ended March 31, 2013, and March 31, 2012 (unaudited)</u>     | 4           |
| <u>Condensed Consolidated Statements of Cash Flows for the Three Months Ended March 31, 2013, and March 31, 2012 (unaudited)</u> | 5           |
| <u>Notes to Interim Condensed Consolidated Financial Statements</u>  | 6           |
| <b><u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u></b>                      | 11          |
| <b><u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u></b>   | 14          |
| <b><u>Item 4. Controls and Procedures</u></b>  | 14          |
| <b><u>PART II - OTHER INFORMATION</u></b>  | 14          |
| <b><u>Item 1A. Risk Factors</u></b>  | 14          |
| <b><u>Item 6. Exhibits</u></b>   | 14          |
| <b><u>SIGNATURES / EXHIBIT INDEX</u></b>   | 15          |
| <b>Exhibits</b>  | 17          |

Table of Contents**PART I: FINANCIAL INFORMATION****ITEM 1: FINANCIAL STATEMENTS****UFP Technologies, Inc.****Condensed Consolidated Balance Sheets**

|   | 31-Mar-13<br>(unaudited) | 31-Dec-12     |
|---|--------------------------|---------------|
| <b>Assets</b>   |                          |               |
| Current assets:   |                          |               |
| Cash and cash equivalents   | \$ 31,941,697            | \$ 33,479,519 |
| Receivables, net  | 18,514,136               | 17,835,902    |
| Inventories   | 10,530,625               | 9,695,060     |
| Prepaid expenses  | 1,540,282                | 653,916       |
| Refundable income taxes   | 936,908                  | 1,713,687     |
| Deferred income taxes   | 1,120,865                | 1,115,959     |
| Total current assets  | 64,584,513               | 64,494,043    |
| Property, plant, and equipment  | 60,820,860               | 59,569,202    |
| Less accumulated depreciation and amortization  | (37,090,839)             | (36,250,906)  |
| Net property, plant, and equipment  | 23,730,021               | 23,318,296    |
| Goodwill  | 7,038,631                | 7,038,631     |
| Intangible assets, net  | 1,950,288                | 2,083,941     |
| Other assets  | 1,764,512                | 1,682,529     |
| Total assets  | \$ 99,067,965            | \$ 98,617,440 |
| <b>Liabilities and Stockholders Equity</b>  |                          |               |
| Current liabilities:  |                          |               |
| Accounts payable  | 4,684,644                | \$ 4,088,003  |
| Accrued expenses  | 5,362,025                | 7,592,842     |
| Current installments of long-term debt  | 1,543,773                | 1,550,190     |
| Total current liabilities   | 11,590,442               | 13,231,035    |
| Long-term debt, excluding current installments  | 8,514,314                | 8,313,709     |
| Deferred income taxes   | 1,591,004                | 1,589,654     |
| Retirement and other liabilities  | 2,297,006                | 2,222,238     |
| Total liabilities   | 23,992,766               | 25,356,636    |
| Commitments and contingencies   |                          |               |
| Stockholders equity:  |                          |               |
| Preferred stock, \$.01 par value. Authorized 1,000,000 shares; no shares issued or outstanding  |                          |               |
| Common stock, \$.01 par value. Authorized 20,000,000 shares; issued and outstanding 6,796,959 at March 31, 2013, and 6,749,913 at December 31, 2012 | 67,970                   | 67,499        |
| Additional paid-in capital  | 19,022,615               | 19,238,934    |
| Retained earnings   | 55,984,614               | 53,954,371    |
| Total UFP Technologies, Inc. stockholders equity  | 75,075,199               | 73,260,804    |
| Total liabilities and stockholders equity   | \$ 99,067,965            | \$ 98,617,440 |

The accompanying notes are an integral part of these condensed consolidated financial statements.



Table of Contents

## UFP Technologies, Inc.

Condensed Consolidated Statements of Income

(Unaudited)

|  | Three Months Ended |               |
|--|--------------------|---------------|
|  | 31-Mar-2013        | 31-Mar-2012   |
| Net sales  | \$ 33,697,014      | \$ 31,952,223 |
| Cost of sales                                      | 24,794,808         | 22,750,861    |
| Gross profit                                       | 8,902,206          | 9,201,362     |
| Selling, general & administrative expenses         | 5,945,949          | 5,518,525     |
| Gain on sale of fixed assets                       |                    | (5,463)       |
| Operating income                                   | 2,956,257          | 3,688,300     |
| Interest expense, net                              | 40,500             | 15,508        |
| Other income (expenses)                            |                    | 2,058         |
| Income before income tax expense                   | 2,915,757          | 3,670,734     |
| Income tax expense                                 | 885,514            | 1,322,000     |
| Net income   | 2,030,243          | 2,348,734     |
| <i>Net income per share</i>                        |                    |               |
| Basic  | \$ 0.30            | \$ 0.36       |
| Diluted  | \$ 0.29            | \$ 0.33       |
| <i>Weighted average common shares outstanding:</i> |                    |               |
| Basic  | 6,768,408          | 6,588,367     |
| Diluted  | 7,087,637          | 7,030,197     |

The accompanying notes are an integral part of these condensed consolidated financial statements.

Table of Contents

## UFP Technologies, Inc.

**Condensed Consolidated Statements of Cash Flows**

(Unaudited)

|   | Three Months Ended   |                      |
|---|----------------------|----------------------|
|   | 31-Mar-2013          | 31-Mar-2012          |
| <b>Cash flows from operating activities:</b>  |                      |                      |
| Net income  | \$ 2,030,243         | \$ 2,348,734         |
| Adjustments to reconcile net income to net cash provided by operating activities:               |                      |                      |
| Depreciation and amortization   | 973,586              | 681,449              |
| Gain on sale of fixed assets  |                      | (5,463)              |
| Share-based compensation  | 179,340              | 186,901              |
| Excess tax benefit on share-based compensation  |                      | (276,596)            |
| Deferred income taxes   | (3,556)              | 58,450               |
| Changes in operating assets and liabilities:  |                      |                      |
| Receivables, net  | (678,234)            | (769,707)            |
| Inventories   | (835,565)            | (307,718)            |
| Taxes receivable  | 776,779              | 676,618              |
| Prepaid expenses  | (886,366)            | (391,291)            |
| Accounts payable  | 596,641              | 611,358              |
| Accrued taxes and other expenses  | (2,030,816)          | (820,443)            |
| Retirement and other liabilities  | 74,768               | 205,323              |
| Other assets  | (81,983)             | (541,299)            |
| <b>Net cash provided by operating activities</b>  | <b>114,837</b>       | <b>1,656,316</b>     |
| <b>Cash flows from investing activities:</b>  |                      |                      |
| Additions to property, plant, and equipment   | (1,251,658)          | (2,309,282)          |
| Holdback payment related to the acquisition of PAC Foam   | (200,000)            |                      |
| Proceeds from sale of fixed assets  |                      | 5,463                |
| Redemption of cash value life insurance   |                      | 131,621              |
| <b>Net cash used in investing activities</b>  | <b>(1,451,658)</b>   | <b>(2,172,198)</b>   |
| <b>Cash flows from financing activities:</b>  |                      |                      |
| Proceeds from the issuance of long-term debt  | 579,650              |                      |
| Principal repayments of long-term debt  | (385,462)            | (145,165)            |
| Proceeds from exercise of stock options, net of attestation                                     | 30,975               | 34,088               |
| Excess tax benefit on share-based compensation  |                      | 276,596              |
| Payment of statutory withholdings for stock options exercised and restricted stock units vested | (426,164)            | (672,284)            |
| Distribution to United Development Company Limited (non-controlling interests)                  |                      | (1,209,732)          |
| <b>Net cash used in financing activities</b>  | <b>(201,001)</b>     | <b>(1,716,497)</b>   |
| Net decrease in cash and cash equivalents   | (1,537,822)          | (2,232,379)          |
| <b>Cash and cash equivalents at beginning of period</b>   | <b>33,479,519</b>    | <b>29,848,798</b>    |
| <b>Cash and cash equivalents at end of period</b>   | <b>\$ 31,941,697</b> | <b>\$ 27,616,419</b> |

The accompanying notes are an integral part of these condensed consolidated financial statements.



Table of Contents

**NOTES TO INTERIM**

**CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

(1) Basis of Presentation

The interim condensed consolidated financial statements of UFP Technologies, Inc. (the Company) presented herein, have been prepared pursuant to the rules of the Securities and Exchange Commission for quarterly reports on Form 10-Q and do not include all the information and note disclosures required by accounting principles generally accepted in the United States of America. These statements should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2012, included in the Company's 2012 Annual Report on Form 10-K as filed with the Securities and Exchange Commission.

The condensed consolidated balance sheet as of March 31, 2013, the condensed consolidated statements of income for the three-month period ended March 31, 2013, and the condensed consolidated statements of cash flows for the three-month period ended March 31, 2013, are unaudited but, in the opinion of management, include all adjustments (consisting of normal, recurring adjustments) necessary for a fair presentation of results for these interim periods.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period.

The results of operations for the three-month period ended March 31, 2013, are not necessarily indicative of the results to be expected for the entire fiscal year ending December 31, 2013.

(2) Supplemental Cash Flow Information

Cash paid for interest and income taxes is as follows:

|                              | <b>Three Months Ended</b> |                  |
|------------------------------|---------------------------|------------------|
|                              | <b>31-Mar-13</b>          | <b>31-Mar-12</b> |
| Interest                     | \$ 39,358                 | \$ 23,008        |
| Income taxes, net of refunds | \$ 114,759                | \$ 242,336       |

During the three-month periods ended March 31, 2013, and 2012, the Company permitted the exercise of stock options with exercise proceeds paid with the Company's stock (cashless exercises) totaling \$0 and \$46,620, respectively.

(3) Fair Value Accounting

The Company has other financial instruments, such as accounts receivable, accounts payable, and accrued expenses, which are stated at carrying amounts that approximate fair value because of the short maturity of those instruments. The carrying amount of the Company's long-term debt approximates fair value as the interest rate on the debt approximates the estimated borrowing rate currently available to the Company.

(4) Share-Based Compensation

Share-based compensation cost is measured at the grant date based on the calculated fair value of the award and is recognized as an expense over the employee's requisite service period (generally the vesting period of the equity grant).

Table of Contents

The Company issues share-based payments through several plans that are described in detail in the notes to the consolidated financial statements for the year ended December 31, 2012. The compensation cost charged against income for those plans is as follows:

|   | Three Months Ended |             |
|---|--------------------|-------------|
|   | 31-Mar-2013        | 31-Mar-2012 |
| Cost of sales                             | \$                 | \$          |
| Selling, general & administrative expense | 179,340            | 186,901     |
| Total share-based compensation expense    | \$ 179,340         | \$ 186,901  |

The total income tax benefit recognized in the condensed consolidated statements of income for share-based compensation arrangements was approximately \$55,000 for each of the three-month periods ended March 31, 2013, and 2012.

The following is a summary of stock option activity under all plans for the three-month period ended March 31, 2013:

|   | Shares Under<br>Options | Weighted<br>Average<br>Exercise Price | Aggregate<br>Intrinsic Value |
|---|-------------------------|---------------------------------------|------------------------------|
| Outstanding at December 31, 2012              | 493,888                 | \$ 5.47                               |                              |
| Granted                                       | 60,000                  | 18.85                                 |                              |
| Exercised                                     | (7,500)                 | 4.13                                  |                              |
| Cancelled or expired                          |                         |                                       |                              |
| Outstanding at March 31, 2013                 | 546,388                 | 6.96                                  | \$ 6,225,706                 |
| Options exercisable at March 31, 2013         | 470,138                 | 5.28                                  | \$ 6,116,693                 |
| Vested and expected to vest at March 31, 2013 | 546,388                 | 6.96                                  | \$ 6,225,706                 |

On March 31, 2013, the Company granted to certain employees options for the purchase of 60,000 shares of its common stock at that day's closing price of \$18.85. The compensation expense was determined as the fair value of the options using the Black Scholes option pricing model based on the following assumptions:

|                         |           |
|-------------------------|-----------|
| Expected volatility     | 40.0%     |
| Expected dividends      | none      |
| Risk free interest rate | 0.4%      |
| Expected term           | 3.8 years |

The stock volatility for each grant is determined based on a review of the experience of the weighted average of historical daily price changes of the Company's common stock over the expected option term, and the risk-free rate is based on the U.S. Treasury yield curve in effect at the time of grant for periods corresponding with the expected life of the option. The weighted average grant date fair value of options granted during the three-month period ended March 31, 2013, was \$5.77.

During the three-month periods ended March 31, 2013, and 2012, the total intrinsic value of all options exercised (i.e., the difference between the market price on the exercise date and the price paid by the employees to exercise the options) was \$114,477 and \$2,028,138, respectively,

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and the total amount of consideration received from the exercised options was \$30,975, and \$80,708, respectively.

During the three-month periods ended March 31, 2013, and 2012, the Company recognized compensation expenses related to stock options granted to directors and employees of \$25,396 and \$18,186, respectively.

On February 18, 2013, the Company's Compensation Committee approved the award of \$400,000 payable in shares of common stock to the Company's Chairman, Chief Executive Officer, and President under the 2003 Incentive Plan. The shares will be issued on or before December 31, 2013. The Company recorded compensation expense associated with the award of \$100,000 during the three-month period ended March 31, 2013. In the three-month period ended March 31, 2012, the Company recorded \$75,000 of compensation expense for a similar award.

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### Table of Contents

The following table summarizes information about Restricted Stock Units ( RSUs ) activity during the three-month period ended March 31, 2013:

|                               | Restricted<br>Stock Units | Weighted Average<br>Award Date<br>Fair Value |
|-------------------------------|---------------------------|--|
| Unvested at December 31, 2012 | 108,866                   | \$ 8.77                                      |
| Awarded                       | 10,600                    | 19.97  |
| Shares vested                 | (61,635)                  | 6.67   |
| Forfeited / cancelled         | (5,679)                   | 16.17  |
| Unvested at March 31, 2013    | 52,152                    | \$ 13.59                                     |

During the three-month periods ended March 31, 2013, and 2012, the Company recorded compensation expense related to RSUs of \$53,944 and \$93,715, respectively.

At its discretion, the Company allows option and RSU holders to surrender previously owned common stock in lieu of paying the minimum statutory withholding taxes due upon the exercise of options or the vesting of RSUs. During the three-month periods ended March 31, 2013, and 2012, 22,089 and 39,707 shares were surrendered at an average market price of \$19.29 and \$16.93, respectively.

March 31, 2013, unrecognized compensation expense of \$1,278,676 is expected to be recognized over a weighted average period of 1.6 years.

#### (5) Inventories

Inventories are stated at the lower of cost (first-in, first-out) or market, and consist of the following at the stated dates:

|                 | 31-Mar-2013   | 31-Dec-2012  |
|-----------------|---------------|--------------|
| Raw materials   | \$ 6,662,512  | \$ 6,260,354 |
| Work in process | 882,020       | 675,228      |
| Finished goods  | 2,986,093     | 2,759,478    |
| Total inventory | \$ 10,530,625 | \$ 9,695,060 |

#### (6) Preferred Stock

On March 18, 2009, the Company declared a dividend of one preferred share purchase right (a Right ) for each outstanding share of common stock, par value \$0.01 per share, to the stockholders of record on March 20, 2009. Each Right entitles the registered holder to purchase from the Company one one-thousandth of a share of Series A Junior Participating Preferred Stock, par value \$0.01 per share (the Preferred Share ) of the Company, at a price of \$25 per one one-thousandth of a Preferred Share subject to adjustment and the terms of the Rights Agreement. The Rights expire on March 19, 2019.

(7) Income Per Share

Basic income per share is based on the weighted average number of shares of common stock outstanding. Diluted income per share is based upon the weighted average of common shares and dilutive common stock equivalent shares outstanding during each period.

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### Table of Contents

The weighted average number of shares used to compute basic and diluted net income per share consisted of the following:

|   | Three Months Ended |             |
|---|--------------------|-------------|
|   | 31-Mar-2013        | 31-Mar-2012 |
| Weighted average common shares outstanding, basic                       | 6,768,408          | 6,588,367   |
| Weighted average common equivalent shares due to stock options and RSUs | 319,229            | 441,830     |
| Weighted average common shares outstanding, diluted                     | 7,087,637          | 7,030,197   |

The computation of diluted earnings per share excludes the effect of the potential exercise of stock awards, including stock options, when the average market price of the common stock is lower than the exercise price of the related options during the period. These outstanding stock awards are not included in the computation of diluted income per share because the effect would have been antidilutive. For the three-month periods ended March 31, 2013, and 2012, the number of stock awards excluded from the computation was 64,337 and 10,000, respectively.

### (8) Segment Reporting

The Company is organized based on the nature of the products and services it offers. Under this structure, the Company produces products within two distinct segments: Engineered Packaging and Component Products. Within the Engineered Packaging segment, the Company primarily uses polyethylene and polyurethane foams, sheet plastics, and pulp fiber to provide customers with cushion packaging for their products. Within the Component Products segment, the Company primarily uses cross-linked polyethylene and technical urethane foams to provide customers in the medical, aerospace and defense, automotive, athletic, and leisure industries with custom-designed products for numerous purposes.

The accounting policies of the segments are the same as those described in Note 1 to the consolidated financial statements contained in the Company's annual report on Form 10-K for the year ended December 31, 2012, as filed with the Securities and Exchange Commission. The Company evaluates the performance of its operating segments based on operating income.

Inter-segment transactions are uncommon and not material. Therefore, they have not been reflected separately in the financial table below. Revenues from customers outside of the United States are not material. No customer comprised more than 5% of the Company's consolidated revenues for the three-month period ended March 31, 2013. All of the Company's assets are located in the United States. Unallocated assets consists of the Company's cash balance.

|                             | Three Months Ended 3/31/13    |                             |                             | Three Months Ended 3/31/12    |                             |                             | Total<br>UFPT<br>\$ |
|-----------------------------|-------------------------------|-----------------------------|-----------------------------|-------------------------------|-----------------------------|-----------------------------|---------------------|
|                             | Engineered<br>Packaging<br>\$ | Component<br>Products<br>\$ | Unallocated<br>Assets<br>\$ | Engineered<br>Packaging<br>\$ | Component<br>Products<br>\$ | Unallocated<br>Assets<br>\$ |                     |
| Net sales                   | 10,865,306                    | 22,831,708                  | 33,697,014                  | 9,617,822                     | 22,334,401                  | 31,952,223                  |                     |
| Operating income            | 193,631                       | 2,762,626                   | 2,956,257                   | 454,656                       | 3,233,644                   | 3,688,300                   |                     |
| Depreciation / amortization | 645,748                       | 327,838                     | 973,586                     | 328,645                       | 352,804                     | 681,449                     |                     |

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|                      |            |            |            |            |            |            |            |            |
|----------------------|------------|------------|------------|------------|------------|------------|------------|------------|
| Capital expenditures | 500,014    | 751,644    |            | 1,251,658  | 1,835,570  | 473,712    |            | 2,309,282  |
| Total assets         | 34,448,170 | 32,678,098 | 31,941,697 | 99,067,965 | 22,038,608 | 30,690,457 | 27,616,419 | 80,345,484 |



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### Table of Contents

#### (9) Other Intangible Assets

The carrying values of the company's definite lived intangible assets as of March 31, 2013, and December 31, 2012, are as follows:

|   | Patents   | Non-competes | Customer list | Total       |
|---|-----------|--------------|---------------|-------------|
| Estimated useful life                         | 14 years  | 5 years      | 5 years       |             |
| Gross amount at March 31, 2013                | 428,806   | 512,000      | 2,306,436     | 3,247,242   |
| Accumulated amortization at March 31, 2013    | (428,806) | (180,701)    | (687,447)     | (1,296,954) |
| Net balance at March 31, 2013                 |           | 331,299      | 1,618,989     | 1,950,288   |
| Gross amount at December 31, 2012             | 428,806   | 512,000      | 2,306,436     | 3,247,242   |
| Accumulated amortization at December 31, 2012 | (428,806) | (156,500)    | (577,995)     | (1,163,301) |
| Net balance at December 31, 2012              |           | 355,500      | 1,728,441     | 2,083,941   |

Amortization expense related to intangible assets was \$133,653 and \$39,951 for the three-month periods ended March 31, 2013, and 2012, respectively. Future amortization will be:

| Remainder of: |              |
|---------------|--------------|
| 2013          | \$ 395,951   |
| 2014          | 444,937      |
| 2015          | 369,800      |
| 2016          | 369,800      |
| 2017          | 369,800      |
| Total         | \$ 1,950,288 |

#### (10) Income Taxes

The income tax expense included in the accompanying unaudited consolidated statements of income principally relates to the Company's proportionate share of the pre-tax income of its majority-owned subsidiaries. The determination of income tax expense for interim reporting purposes is based upon the estimated effective tax rate for the year adjusted for the impact of any discrete items which are accounted for in the period in which they occur.

The Company recorded a tax expense of approximately 30.4% of income before income tax expense for the three month period ended March 31, 2013, compared to a tax expense of approximately 36% for the comparable three-month period in 2012. The effective tax rate for the quarter ended March 31, 2013 includes a discrete event for a retroactive application for a 2012 research and development credit. The American Taxpayer Relief Act of 2012 was passed by Congress and signed into law on January 1, 2013. The provisions under this law are to be applied retroactively to January 1, 2012. As a result of the law being signed on January 1, 2013, the financial impact of the retroactive provision was recorded as a discrete event in the first quarter of 2013. The Company recorded a reduction to tax expense in the first quarter of 2013 by \$135,000. Excluding this discrete event, the effective tax rate for the quarter ended March 31, 2013 was 35%.

(11) Acquisition

On December 31, 2012, the Company acquired substantially all of the assets of Packaging Alternatives Corporation ( PAC ), a Costa Mesa, California-based, foam fabricator for \$5.7 million. The Consolidated Statement of Income for the three-month period ended March 31, 2013, include the following results for PAC:

|                  |    |           |
|------------------|----|-----------|
| Sales            | \$ | 2,681,704 |
| Operating Income | \$ | 66,546    |

Table of Contents

**ITEM 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

**Forward-looking Statements**

This report contains certain statements that are forward-looking statements as that term is defined under the Private Securities Litigation Reform Act of 1995 and releases issued by the Securities and Exchange Commission. The words believe, expect, anticipate, intend, plan, estimate, and other expressions, which are predictions of or indicate future events and trends and that do not relate to historical matters, identify forward-looking statements. Examples of forward-looking statements included in this report include, without limitation, statements regarding the anticipated financial performance and/or future business prospects of the Company, anticipated trends in the different markets in which the Company competes, including the molded fiber, medical and military markets, anticipated advantages the Company expects to realize from its investments and capital expenditures, including the development of and investments in its molded fiber product line, expectations regarding the manufacturing capacity of the Company's new production equipment, anticipated advantages relating to the Company's decision to cease operations at its Ventura, California plant and to consolidate manufacturing in other facilities, expected methods of growth for the Company, and the overall economy.

Forward-looking statements involve known and unknown risks, uncertainties and other factors, which may cause the actual results, performance, or achievements of the Company to differ materially from anticipated future results, performance, or achievements expressed or implied by such forward-looking statements. Other examples of these risks, uncertainties, and other factors include, without limitation, the following: economic conditions that affect sales of the products of the Company's customers, risks associated with the identification of suitable acquisition candidates and the successful, efficient execution and integration of such acquisitions, the implementation of new production equipment in a timely, cost-efficient manner, risks that any benefits from such new equipment may be delayed or not fully realized, or that the Company may be unable to fully utilize its expected production capacity, actions by the Company's competitors, and the ability of the Company to respond to such actions, the ability of the Company to obtain new customers, the ability of the Company to offset lost revenues, evolving customer requirements, difficulties associated with the roll-out of new products, decisions by customers to cancel or defer orders for the Company's products that previously had been accepted, risks and uncertainties associated with plant closures and expected efficiencies from consolidating manufacturing, risks associated with the internal reorganization of our sales and engineering groups, the costs of compliance with the requirements of Sarbanes-Oxley, and general economic and industry conditions and other factors. In addition to the foregoing, the Company's actual future results could differ materially from those projected in the forward-looking statements as a result of the risk factors set forth elsewhere in this report and changes in general economic conditions, interest rates and the assumptions used in making such forward-looking statements. All of the forward-looking statements are qualified in their entirety by reference to the risk factors and other disclaimers described in the Company's filings with the Securities and Exchange Commission, in particular its most recent Annual Report on Form 10-K. The Company undertakes no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise.

**Overview**

Using foams, plastics, composites and natural fiber materials, UFP Technologies designs and manufactures a vast range of solutions primarily for the medical, automotive, aerospace and defense, and packaging markets.

Sales to the automotive industry started slowly in 2013 due to temporary holiday plant shutdowns at certain UFP customers. This sales decline, coupled with anticipated soft demand in the aerospace and defense market due to cuts in government spending, offset strong sales to the medical market. Sales for the three-month period ended March 31, 2013 increased 5.5% over the comparable period in 2012. However, excluding the

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sales of the newly acquired PAC operations in Costa Mesa, California, sales decreased 2.9%. The impact of this, coupled with approximately \$150,000 in one-time costs incurred in integrating the PAC operations and absorbing the beauty business in El Paso, Texas, caused a 13.5% reduction in net income for the first quarter of 2013, compared to the first quarter of 2012. The Company considers the acquisition of PAC and the closure of its Ventura plant and movement of its business to other UFP plants as key strategic investments that it expects to benefit future periods.

The Company's current strategy includes organic growth and growth through strategic acquisitions.

Details regarding the Company's segment results of operations are described in Note 8 to the consolidated financial statements included in Item 1 of this Form 10-Q.

Table of Contents

**Sales**

Sales for the three-month period ended March 31, 2013, increased approximately 5.5% to \$33.7 million from sales of \$32.0 million for the same period in 2012. Sales for the first quarter at the Company's newly acquired operations in Costa Mesa, CA were approximately \$2.7 million. Absent these sales the Company's sales declined 2.9% for the quarter. The increase in sales for the three-month period ended March 31, 2013, is primarily due to increased sales to the medical industry of approximately \$3.4 million (Component Products segment), mostly due to sales at PAC, largely offset by declines in sales to the automotive market (Component Products segment) and aerospace and defense (both the Component Products and Packaging segments) of approximately \$1.1 million and \$525,000, respectively.

**Gross Profit**

Gross profit as a percentage of sales ( gross margin ) decreased to 26.4% for the three-month period ended March 31, 2013, from 28.8% in the same period in 2012. The decrease in gross margin for the three-month period ended March 31, 2013, is primarily due to higher material content on sales of product from the newly acquired PAC operations of approximately \$475,000 or 1.4% of sales (Component Products segment) as well as the impact of the fixed portion of overhead on lower sales (absent PAC sales) of 1.0% of sales (both the Component Products and Packaging segments).

**Selling, General and Administrative Expenses**

Selling, general, and administrative expenses ( SG&A ) increased approximately \$427,000 or 7.7% to \$5.9 million for the three-month period ended March 31, 2013, from \$5.5 million for the same period in 2012. The increase in SG&A is primarily due to SG&A of the PAC operations of approximately \$500,000 (Component Products segment).

As a percentage of sales, SG&A increased slightly to 17.6% for the three-month period ended March 31, 2013, from 17.3% for the same three-month period in 2012. The increase in SG&A as a percentage of sales for the three-month period ended March 31, 2013, is primarily due to the reduction in sales absent sales of PAC.

**Other Expenses**

The Company had net interest expense of approximately \$41,000 for the three-month period ended March 31, 2013, compared to net interest expense of approximately \$16,000 in the same period of 2012. The increase in interest expense for the three-month period ended March 31, 2013, is primarily due to lower interest earned on cash and incremental term loans taken by the Company in 2012 to finance Molded Fiber equipment.

## Income Taxes

The Company recorded a tax expense of approximately 30.4% of income before income tax expense for the three-month period ended March 31, 2013, compared to a tax expense of approximately 36% for the comparable three-month period in 2012. The decrease in the effective income tax rate for the three-month period ended March 31, 2013, is primarily due to an expected research and development tax credit the in the Company's 2012 tax returns, that was not reflected in the 2012 operating results because the R&D tax credits had expired as of December 31, 2012, but were extended by legislation passed in 2013.

## Liquidity and Capital Resources

The Company funds its operating expenses, capital requirements, and growth plan through internally generated cash and bank credit facilities.

At March 31, 2013, and December 31, 2012, the Company's working capital was approximately \$53.0 million and \$51.3 million, respectively. The increase in working capital for the three-month period ended March 31, 2013, is primarily due to an increase in inventory of approximately \$835,000 primarily due to the timing of raw material purchases and an increase in receivables, net of approximately \$678,000 due to strong March sales.

Net cash provided by operations for the three-month period ended March 31, 2013, was approximately \$115,000, primarily due to net income of approximately \$2.0 million and depreciation and amortization of approximately \$974,000, offset by a reduction in accrued expenses of approximately \$2.2 million due to the payment in the first quarter of year-end bonuses, an annual profit sharing contribution and certain income tax payments.

Table of Contents

Cash used in investing activities during the three-month period ended March 31, 2013, was approximately \$1.5 million and was primarily the result of additions of manufacturing machinery and equipment.

Cash used in financing activities was approximately \$200,000 in the three-month period ended March 31, 2013, representing cash used to service term debt and to pay statutory withholding for restricted stock units vested of approximately \$810,000 partially offset by proceeds from the issuance of term debt of approximately \$580,000.

On January 29, 2009, the Company amended and extended its credit facility with Bank of America, NA. The facility comprises: (i) a revolving credit facility of \$17 million; (ii) a term loan of \$2.1 million with a seven-year straight line amortization; (iii) a mortgage loan of \$1.8 million with a 20-year straight line amortization; and (iv) a mortgage loan of \$4.0 million with a 20-year straight line amortization. Extensions of credit under the revolving credit facility are based in part upon accounts receivable and inventory levels. Therefore, the entire \$17 million may not be available to the Company. At March 31, 2013, the Company had no borrowings outstanding and availability of approximately \$16.9 million, based upon collateral levels as of that date. The credit facility calls for interest of LIBOR plus a margin that ranges from 1.0% to 1.5% or, at the option of the Company, the bank's prime rate less a margin that ranges from 0.25% to zero. In both cases the applicable margin is dependent upon Company performance. The loans are collateralized by a first priority lien on all of the Company's assets, including its real estate located in Georgetown, Massachusetts, and in Grand Rapids, Michigan. Under the credit facility, the Company is subject to a minimum fixed charge coverage financial covenant with which it was in compliance at March 31, 2013. The Company's \$17 million revolving credit facility matures November 30, 2013, and the term loans are due January 29, 2016. The Company anticipates negotiating an extension of this facility. The Company cannot assure that such extension will be completed on favorable terms or on a timely basis, if at all. The interest rate on these facilities was approximately 1.2% at March 31, 2013, and there were no borrowings outstanding on the line of credit.

On October 11, 2012, the Company entered a loan agreement with US Bank Equipment Finance to finance the purchase of two new molded fiber machines, both of which are operational. The annual interest rate is fixed at 1.83%. As of March 31, 2013, the outstanding balance is approximately \$4.6 million. The loan will be repaid over a five-year term. The loan is secured by the related molded fiber machines.

Throughout 2013, the Company plans to continue to add capacity to enhance operating efficiencies in its manufacturing plants. The Company may consider additional acquisitions of companies, technologies, or products that are complementary to its business. The Company believes that its existing resources, including its revolving credit facility, together with cash generated from operations and funds expected to be available to it through any necessary equipment financing and additional bank borrowings, will be sufficient to fund its cash flow requirements, including capital asset acquisitions, through the next twelve months.

**Commitments, Contractual Obligations, and Off-Balance Sheet Arrangements**

The following table summarizes the Company's commitments, contractual obligations, and off balance sheet arrangements at March 31, 2013, and the effect such obligations are expected to have on its liquidity and cash flow in future periods:

| Total | Less than<br>1 Year | Payment Due By Period |              | More than<br>5 Years |
|-------|---------------------|-----------------------|--------------|----------------------|
|       |                     | 1-3<br>Years          | 3-5<br>Years |                      |

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|                         |    |            |    |           |    |           |    |           |           |           |
|-------------------------|----|------------|----|-----------|----|-----------|----|-----------|-----------|-----------|
| Term Loans              | \$ | 841,052    | \$ | 216,270   | \$ | 576,720   | \$ | 48,062    | \$        |           |
| Equipment Loans         |    | 4,564,594  |    | 720,420   |    | 1,971,597 |    | 1,872,577 |           |           |
| Grand Rapids Mortgage   |    | 3,183,333  |    | 150,001   |    | 400,002   |    | 400,001   | 2,233,329 |           |
| Massachusetts Mortgage  |    | 1,469,108  |    | 69,225    |    | 184,600   |    | 184,600   | 1,030,683 |           |
| Operating Leases        |    | 6,538,561  |    | 1,515,859 |    | 2,958,204 |    | 2,064,498 |           |           |
| Debt interest           |    | 887,117    |    | 161,495   |    | 371,149   |    | 247,671   | 106,802   |           |
| Supplemental Retirement |    | 227,083    |    | 56,250    |    | 70,833    |    | 50,000    | 50,000    |           |
| Total                   | \$ | 17,710,848 | \$ | 2,889,520 | \$ | 6,533,105 | \$ | 4,867,409 | \$        | 3,420,814 |

The Company requires cash to pay its operating expenses, purchase capital equipment, and to service the obligations listed above. The Company's principal sources of funds are its operations and its revolving credit facility.



Table of Contents

Although the Company generated cash from operations during the three-month period ended March 31, 2013, it cannot guarantee that its operations will generate cash in future periods.

The Company had no off balance sheet arrangements during the three-month period ended March 31, 2013, other than operating leases.

**ITEM 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The following discussion of the Company's market risk includes forward-looking statements that involve risk and uncertainties. Actual results could differ materially from those projected in the forward-looking statements. Market risk represents the risk of changes in value of a financial instrument caused by fluctuations in interest rates, foreign exchange rates, and equity prices. At March 31, 2013, the Company's cash and cash equivalents consisted of bank accounts in U.S. dollars, and their valuation would not be affected by market risk. The Company has several debt instruments where interest is based upon either the prime rate or LIBOR and, therefore, future operations could be affected by interest rate changes. However, the Company believes that the market risk of the debt is minimal.

**ITEM 4: CONTROLS AND PROCEDURES**

As of the end of the period covered by this report, the Company's Chief Executive Officer and Chief Financial Officer performed an evaluation of the effectiveness of the Company's disclosure controls and procedures (as defined in SEC Rule 13a-15(e) or 15d-15(e)). Based upon that evaluation, they concluded that the Company's disclosure controls and procedures were effective to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission's rules and forms.

There has been no change in the Company's internal control over financial reporting during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

**PART II: OTHER INFORMATION**

**ITEM 1A: RISK FACTORS**

Information regarding risk factors appears in Part I Item 2 of this Form 10-Q in Management's Discussion and Analysis of Financial Condition and Results of Operations under Forward-Looking Statements and in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2012, in Part I Item 1A under Risk Factors. There have been no material changes from the risk factors previously disclosed in Item 1A of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2012.

**ITEM 6: EXHIBITS**

The following exhibits are included herein:

| <b>Exhibit No.</b> | <b>Description</b>   |
|--------------------|--|
| 10.62              | Amendment No. 2 to Employment Agreement with R. Jeffrey Bailly (incorporated by reference to the Company's Report on Form 8-K dated February 22, 2013. The number set forth herein is the number of the Exhibit in said Report). |
| 10.63              | Form of 2013 CEO Stock Unit Award Agreement (incorporated by reference to the Company's Report on Form 8-K dated February 22, 2013. The number set forth herein is the number of the Exhibit in said Report).                    |
| 10.64              | Form of 2013 Stock Unit Award Agreement (incorporated by reference to the Company's Report on Form 8-K dated February 22, 2013. The number set forth herein is the number of the Exhibit in said Report).                        |

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## Table of Contents

| <b>Exhibit No.</b> | <b>Description</b>   |
|--------------------|--|
| 10.65              | UFP Technologies, Inc. 2003 Incentive Plan, as amended.*   |
| 10.66              | 2009 Non-Employee Director Stock Incentive Plan, as amended.*  |
| 31.1               | Rule 13a-14(a)/15d-14(a) Certification of the Chief Executive Officer.*  |
| 31.2               | Rule 13a-14(a)/15d-14(a) Certification of the Chief Financial Officer.*  |
| 32                 | Certification pursuant to 18 U.S.C., Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.** |
| 101.INS            | XBRL Instance Document.***   |
| 101.SCH            | XBRL Taxonomy Extension Schema Document.***  |
| 101.CAL            | XBRL Taxonomy Calculation Linkbase Document.***  |
| 101.LAB            | XBRL Taxonomy Label Linkbase Document.***  |
| 101.PRE            | XBRL Taxonomy Presentation Linkbase Document.***   |
| 101.DEF            | XBRL Taxonomy Extension Definition Linkbase Document.***   |

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- \* Filed herewith.  
\*\* Furnished herewith.  
\*\*\* Submitted electronically herewith. Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933 or Section 18 of the Securities Exchange Act of 1934.

## **SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

UFP TECHNOLOGIES, INC.

|       |              |     |   |
|-------|--------------|-----|---|
| Date: | May 10, 2013 | By: | /s/ R. Jeffrey Bailly<br>R. Jeffrey Bailly<br>Chairman, Chief Executive Officer, President, and Director<br>(Principal Executive Officer) |
| Date: | May 10, 2013 | By: | /s/ Ronald J. Lataille<br>Ronald J. Lataille<br>Chief Financial Officer<br>(Principal Financial Officer)                                  |

Table of Contents

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- \* Filed herewith.
  - \*\* Furnished herewith.
  - \*\*\* Submitted electronically herewith. Pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933 or Section 18 of the Securities Exchange Act of 1934.