

CSP INC /MA/
Form 10-Q
February 14, 2013

United States
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended December 31, 2012

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 0-10843

CSP Inc.

(Exact name of Registrant as specified in its Charter)

Massachusetts
(State of incorporation)

04-2441294
(I.R.S. Employer Identification No.)

43 Manning Road
Billerica, Massachusetts 01821-3901
(978) 663-7598
(Address and telephone number of principal executive offices)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§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):

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Large accelerated filer Accelerated filer

Non-accelerated filer (Do not check if a smaller reporting company) 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

As of February 11, 2013, the registrant had 3,442,842 shares of common stock issued and outstanding.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

CSP INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(Amounts in thousands, except par value)

	December 31, 2012 (Unaudited)	September 30, 2012
ASSETS		
Current assets:		
Cash and cash equivalents	\$17,715	\$20,493
Accounts receivable, net of allowances of \$195 and \$243	16,438	12,145
Officer life insurance settlement receivable	—	2,172
Inventories	5,710	6,276
Refundable income taxes	108	121
Deferred income taxes	1,339	1,284
Other current assets	3,188	2,215
Total current assets	44,498	44,706
Property, equipment and improvements, net	1,036	991
Other assets:		
Intangibles, net	472	492
Deferred income taxes	2,376	2,373
Cash surrender value of life insurance	2,208	2,181
Other assets	224	323
Total other assets	5,280	5,369
Total assets	\$50,814	\$51,066
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	\$13,832	\$13,574
Deferred revenue	3,729	3,693
Pension and retirement plans	723	717
Income taxes payable	51	184
Total current liabilities	18,335	18,168
Pension and retirement plans	9,489	9,431
Other long term liabilities	437	426
Total liabilities	28,261	28,025
Commitments and contingencies		
Shareholders' equity:		
Common stock, \$.01 par value per share; authorized, 7,500 shares; issued and outstanding 3,443 and 3,399 shares, respectively	34	34
Additional paid-in capital	10,905	10,875
Retained earnings	18,170	18,744

Accumulated other comprehensive loss	(6,556)	(6,612)
Total shareholders' equity	22,553		23,041	
Total liabilities and shareholders' equity	\$50,814		\$51,066	

See accompanying notes to unaudited consolidated financial statements.

CSP INC. AND SUBSIDIARIES
 UNAUDITED CONSOLIDATED STATEMENTS OF OPERATIONS
 (Amounts in thousands, except for per share data)

	For the three months ended	
	December 31, 2012	December 31, 2011
Sales:		
Product	\$15,305	\$15,154
Services	5,565	5,939
Total sales	20,870	21,093
Cost of sales:		
Product	13,224	12,766
Services	3,469	3,504
Total cost of sales	16,693	16,270
Gross profit	4,177	4,823
Operating expenses:		
Engineering and development	444	383
Selling, general and administrative	3,560	3,676
Total operating expenses	4,004	4,059
Operating income	173	764
Other income (expense):		
Foreign exchange gain (loss)	13	(16)
Other income (expense), net	46	(18)
Total other income (expense), net	59	(34)
Income before income taxes	232	730
Income tax expense	117	269
Net income	\$115	\$461
Net income attributable to common stockholders	\$113	\$454
Net income per share – basic	\$0.03	\$0.14
Weighted average shares outstanding – basic	3,363	3,357
Net income per share – diluted	\$0.03	\$0.13
Weighted average shares outstanding – diluted	3,407	3,395

See accompanying notes to unaudited consolidated financial statements.

CSP INC. AND SUBSIDIARIES
UNAUDITED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(Amounts in thousands)

	For the three months ended	
	December 31, 2012	December 31, 2011
Net income	\$115	\$461
Other comprehensive income (loss):		
Foreign currency translation gain (loss) adjustments	56	(114)
Other comprehensive income (loss)	56	(114)
Total comprehensive income	\$171	\$347

See accompanying notes to unaudited consolidated financial statements.

CSP INC. AND SUBSIDIARIES
 UNAUDITED CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY
 For the Three Months Ended December 31, 2012:
 (Amounts in thousands)

	Shares	Amount	Additional Paid-in Capital	Retained Earnings	Accumulated other comprehensive loss	Total Shareholders' Equity
Balance as of September 30, 2012	3,399	\$ 34	\$ 10,875	\$ 18,744	\$ (6,612)	\$ 23,041
Net income	—	—	—	115	—	115
Other comprehensive income:	—	—	—	—	56	56
Stock-based compensation	—	—	2	—	—	2
Restricted stock issuance	44	—	28	—	—	28
Cash dividends on common stock (\$0.20 per share)	—	—	—	(689)	—	(689)
Balance as of December 31, 2012	3,443	\$ 34	\$ 10,905	\$ 18,170	\$ (6,556)	\$ 22,553

See accompanying notes to unaudited consolidated financial statements.

CSP INC. AND SUBSIDIARIES
 UNAUDITED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (Amounts in thousands)

	For the three months ended	
	December 31, 2012	December 31, 2011
Cash flows from operating activities:		
Net income	\$115	\$461
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	102	89
Amortization of intangibles	21	21
Gain on sale of fixed assets, net	(17)	—
Foreign exchange (gain) loss	(13)	16
Non-cash changes in accounts receivable	(49)	9
Stock-based compensation expense on stock options and restricted stock awards	30	37
Deferred income taxes	(42)	65
Increase in cash surrender value of life insurance	(26)	(27)
Changes in operating assets and liabilities:		
Increase in accounts receivable	(4,101)	(4,397)
Decrease in officer life insurance receivable	2,172	—
Decrease in inventories	573	1,734
Decrease in refundable income taxes	16	23
Increase in other current assets	(691)	(811)
(Increase) decrease in other assets	(135)	16
Increase in accounts payable and accrued expenses	150	695
Increase (decrease) in deferred revenue	(28)	1,047
Decrease in pension and retirement plans liability	(66)	(27)
Increase (decrease) in income taxes payable	(134)	99
Increase in other long term liabilities	10	7
Net cash used in operating activities	(2,113)	(943)
Cash flows from investing activities:		
Life insurance premiums paid	(2)	(80)
Proceeds from the sale of fixed assets	17	—
Purchases of property, equipment and improvements	(135)	(85)
Net cash used in investing activities	(120)	(165)
Cash flows from financing activities:		
Dividends paid	(689)	—
Purchase of common stock	—	(58)
Net cash used in financing activities	(689)	(58)
Effects of exchange rate on cash	144	(71)
Net decrease in cash and cash equivalents	(2,778)	(1,237)
Cash and cash equivalents, beginning of period	20,493	15,874
Cash and cash equivalents, end of period	\$17,715	\$14,637
Supplementary cash flow information:		

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Cash paid for income taxes	\$303	\$99
Cash paid for interest	\$85	\$85

See accompanying notes to unaudited consolidated financial statements.

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CSP INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
THREE MONTHS ENDED DECEMBER 31, 2012 AND 2011

Organization and Business

CSP Inc. was founded in 1968 and is based in Billerica, Massachusetts. To meet the diverse requirements of its industrial, commercial and defense customers worldwide, CSP Inc. and its subsidiaries (collectively “CSPI” or the “Company”) develop and market IT integration solutions and high-performance cluster computer systems. The Company operates in two segments, its Systems segment and its Service and System Integration segment.

1. Basis of Presentation

The accompanying consolidated financial statements have been prepared by the Company, without audit, and reflect all adjustments which, in the opinion of management, are necessary for a fair statement of the results of the interim periods presented. All adjustments were of a normal recurring nature. Certain information and footnote disclosures normally included in the annual financial statements, which are prepared in accordance with accounting principles generally accepted in the United States, have been condensed or omitted. Accordingly, the Company believes that although the disclosures are adequate to make the information presented not misleading, the unaudited financial statements should be read in conjunction with the footnotes contained in the Company’s Annual Report on Form 10-K for the fiscal year ended September 30, 2012.

2. Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States 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. Actual results may differ from those estimates under different assumptions or conditions.

3. Earnings Per Share of Common Stock

Basic net income per common share is computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding for the period. Diluted net income per common share reflects the maximum dilution that would have resulted from the assumed exercise and share repurchase related to dilutive stock options and is computed by dividing net income by the assumed weighted average number of common shares outstanding.

We are required to present earnings per share, or EPS, utilizing the two class method because we had outstanding, non-vested share-based payment awards that contain non-forfeitable rights to dividends or dividend equivalents, which are considered participating securities.

Basic and diluted earnings per share computations for the Company’s reported net income attributable to common stockholders are as follows:

	For the three months ended	
	December 31, 2012	December 31, 2011
	(Amounts in thousands except per share data)	
Net income	\$115	\$461
Less: Net income attributable to nonvested common stock	2	7
Net income attributable to common stockholders	\$113	\$454
Weighted average total shares outstanding – basic	3,426	3,410
Less: weighted average non-vested shares outstanding	63	53
Weighted average number of common shares outstanding – basic	3,363	3,357
Potential common shares from non-vested stock awards and the assumed exercise of stock options	44	38
Weighted average common shares outstanding – diluted	3,407	3,395
Net income per share – basic	\$0.03	\$0.14
Net income per share – diluted	\$0.03	\$0.13

All anti-dilutive securities, including certain stock options, are excluded from the diluted income per share computation. For the three months ended December 31, 2012 and 2011, 197,000 and 205,000 options, respectively, were excluded from the diluted income per share calculation because their inclusion would have been anti-dilutive.

4. Inventories

Inventories consist of the following:

	December 31, 2012	September 30, 2012
	(Amounts in thousands)	
Raw materials	\$942	\$941
Work-in-process	1,318	1,407
Finished goods	3,450	3,928
Total	\$5,710	\$6,276

Finished goods includes inventory that has been shipped, but for which all revenue recognition criteria has not been met, of approximately \$0.4 million and \$1.4 million as of December 31, 2012 and September 30, 2012, respectively.

Total inventory balances in the table above are shown net of reserves for obsolescence of approximately \$4.5 million and \$4.4 million as of December 31, 2012 and September 30, 2012, respectively.

5. Accumulated Other Comprehensive Income (Loss)

The components of accumulated other comprehensive loss are as follows:

	December 31, 2012	September 30, 2012
	(Amounts in thousands)	
Cumulative effect of foreign currency translation	\$ (2,217)	\$ (2,273)
Additional minimum pension liability	(4,339)	(4,339)
Accumulated other comprehensive loss	\$ (6,556)	\$ (6,612)

6. Pension and Retirement Plans

The Company has defined benefit and defined contribution plans in the United Kingdom, Germany and the U.S. In the United Kingdom and Germany, the Company provides defined benefit pension plans and defined contribution plans for the majority of its employees. In the U.S., the Company provides benefits through supplemental retirement plans to certain current and former employees. The domestic supplemental retirement plans have life insurance policies which are not plan assets but were purchased by the Company as a vehicle to fund the costs of the plan. Domestically, the Company also provides for officer death benefits through post-retirement plans to certain officers. All of the Company's defined benefit plans are closed to newly hired employees and have been for the two years ended September 30, 2012 and for the three months ended December 31, 2012.

The Company funds its pension plans in amounts sufficient to meet the requirements set forth in applicable employee benefits laws and local tax laws. Liabilities for amounts in excess of these funding levels are accrued and reported in the consolidated balance sheets.

Our pension plan in the United Kingdom is the only plan with plan assets. The plan assets consist of an investment in a commingled fund which in turn comprises a diversified mix of assets including corporate equity securities, government securities and corporate debt securities.

The components of net periodic benefit costs related to the U.S. and international plans are as follows:

	For the Three Months Ended December 31,					
	Foreign	2012 U.S.	Total	Foreign	2011 U.S.	Total
(Amounts in thousands)						
Pension:						
Service cost	\$15	\$—	\$15	\$16	\$3	\$19
Interest cost	173	16	189	179	21	200
Expected return on plan assets	(104)	—	(104)	(104)	—	(104)
Amortization of:						
Prior service gain	—	—	—	—	—	—
Amortization of net gain	36	6	42	22	7	29
Net periodic benefit cost	\$120	\$22	\$142	\$113	\$31	\$144
Post Retirement:						
Service cost	\$—	\$—	\$—	\$—	\$—	\$—
Interest cost	—	9	9	—	18	18
Amortization of net gain	—	(46)	(46)	—	17	17
Net periodic benefit cost	\$—	\$(37)	\$(37)	\$—	\$35	\$35

7. Segment Information

The following table presents certain operating segment information.

For the Three Months Ended December 31,	Systems Segment	Service and System Integration Segment				Consolidated Total
		Germany	United Kingdom	U.S.	Total	
(Amounts in thousands)						
2012						
Sales:						
Product	\$96	\$2,064	\$154	\$12,991	\$15,209	\$15,305
Service	957	3,204	302	1,102	4,608	5,565
Total sales	1,053	5,268	456	14,093	19,817	20,870
Profit (loss) from operations	(373)	(147)	—	693	546	173
Assets	16,914	13,527	3,524	16,849	33,900	50,814
Capital expenditures	41	55	3	36	94	135
Depreciation and amortization	37	42	5	39	86	123
2011						
Sales:						
Product	\$1,239	\$3,851	\$353	\$9,711	\$13,915	\$15,154
Service	1,107	3,587	316	929	4,832	5,939
Total sales	2,346	7,438	669	10,640	18,747	21,093
Profit from operations	12	275	26	451	752	764
Assets	13,214	16,212	3,727	11,660	31,599	44,813
Capital expenditures	29	26	19	11	56	85
Depreciation and amortization	23	39	7	41	87	110

Profit (loss) from operations consists of sales less cost of sales, engineering and development, selling, general and administrative expenses but is not affected by either non-operating charges/income or by income taxes. Non-operating charges/income consists principally of investment income and interest expense. All intercompany transactions have been eliminated.

The following table lists customers from which the Company derived revenues in excess of 10% of total revenues for the three month periods ended December 31, 2012, and 2011.

	For the three months ended			
	December 31, 2012		December 31, 2011	
	Amount	% of Revenues	Amount	% of Revenues
Customer A	\$ 5.1	24 %	\$ 5.2	25 %
Customer B	\$ 2.6	12 %	\$ 4.5	21 %

8. Fair Value Measures

Assets and Liabilities measured at fair value on a recurring basis are as follows:

Fair Value Measurements Using

	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	Total Balance	Gain or (loss)
As of December 31, 2012 (Amounts in thousands)					
Assets:					
Money Market funds	\$ 3,499	\$ —	\$ —	\$ 3,499	\$ —
Total assets measured at fair value	\$ 3,499				