

UFP TECHNOLOGIES INC  
Form 10-Q  
May 12, 2014  
[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, 2014

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.**

Edgar Filing: UFP TECHNOLOGIES INC - Form 10-Q

(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

6,999,338 shares of registrant's Common Stock, \$0.01 par value, were outstanding as of April 30, 2014.



Table of Contents

**UFP Technologies, Inc.**

**Index**

	<b>Page</b>
<b><u>PART I - FINANCIAL INFORMATION</u></b>	<b>3</b>
<u>Item 1. Financial Statements</u>	3
<u>Condensed Consolidated Balance Sheets as of March 31, 2014 (unaudited) and December 31, 2013</u>	3
<u>Condensed Consolidated Statements of Income for the Three Months Ended March 31, 2014 and March 31, 2013 (unaudited)</u>	4
<u>Condensed Consolidated Statements of Cash Flows for the Three Months Ended March 31, 2014 and March 31, 2013 (unaudited)</u>	5
<u>Notes to Interim Condensed Consolidated Financial Statements</u>	6
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	11
<u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u>	14
<u>Item 4. Controls and Procedures</u>	14
<b><u>PART II - OTHER INFORMATION</u></b>	<b>15</b>
<u>Item 1A. Risk Factors</u>	15
<u>Item 6. Exhibits</u>	15
<u>Signatures</u>	16
<u>Exhibit Index</u>	16

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

(In thousands, except share data)

	March 31, 2014 (Unaudited)	December 31, 2013
<b>Assets</b>		
Current assets:		
Cash and cash equivalents	\$ 34,620	\$ 37,303
Receivables, less allowance for doubtful accounts of \$515 at March 31, 2014 and \$512 at December 31, 2013	18,150	17,032
Inventories	12,177	11,048
Prepaid expenses	2,062	690
Refundable income taxes	949	1,537
Deferred income taxes	1,248	1,222
Total current assets	69,206	68,832
Property, plant, and equipment	65,951	64,574
Less accumulated depreciation and amortization	(40,079)	(39,067)
Net property, plant, and equipment	25,872	25,507
Goodwill	7,322	7,322
Intangible assets, net	1,227	1,346
Other assets	2,064	2,013
Total assets	\$ 105,691	\$ 105,020
<b>Liabilities and Stockholders Equity</b>		
Current liabilities:		
Accounts payable	\$ 4,648	\$ 3,081
Accrued expenses	5,717	8,265
Current installments of long-term debt	980	976
Total current liabilities	11,345	12,322
Long-term debt, excluding current installments	2,620	2,867
Deferred income taxes	2,341	2,436
Retirement and other liabilities	1,525	1,805
Total liabilities	17,831	19,430
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$.01 par value. Authorized 1,000,000 shares; zero shares issued or outstanding		
Common stock, \$.01 par value. Authorized 20,000,000 shares; issued and outstanding 6,996,838 at March 31, 2014 and 6,900,683 at December 31, 2013	70	69
Additional paid-in capital	20,498	20,291
Retained earnings	67,292	65,230
Total stockholders' equity	87,860	85,590
Total liabilities and stockholders' equity	\$ 105,691	\$ 105,020

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

Table of Contents**UFP Technologies, Inc.****Condensed Consolidated Statements of Income**

(In thousands, except share data)

(Unaudited)

	<b>Three Months Ended</b>	
	<b>March 31,</b>	
	<b>2014</b>	<b>2013</b>
Net sales	\$ 34,609	\$ 33,697
Cost of sales	25,580	24,795
Gross profit	9,029	8,902
Selling, general & administrative expenses	5,834	5,946
Operating income	3,195	2,956
Interest expense, net	22	40
Income before income tax expense	3,173	2,916
Income tax expense	1,111	886
Net income	\$ 2,062	\$ 2,030
<i>Net income per share:</i>		
Basic	\$ 0.30	\$ 0.30
Diluted	\$ 0.29	\$ 0.29
<i>Weighted average common shares outstanding:</i>		
Basic	6,972	6,768
Diluted	7,148	7,088

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**

(In thousands)

(Unaudited)

	<b>Three Months Ended March 31,</b>	
	<b>2014</b>	<b>2013</b>
<b>Cash flows from operating activities:</b>		
Net income	\$ 2,062	\$ 2,030
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	1,131	974
Share-based compensation	265	179
Excess tax benefit on share-based compensation	(563)	
Deferred income taxes	(121)	(4)
Changes in operating assets and liabilities:		
Receivables, net	(1,118)	(678)
Inventories	(1,129)	(836)
Prepaid expenses	(1,372)	(886)
Refundable income taxes	1,151	777
Other assets	(51)	(82)
Accounts payable	1,567	597
Accrued expenses	(2,548)	(2,031)
Retirement and other liabilities	(280)	75
<b>Net cash (used in) provided by operating activities</b>	<b>(1,006)</b>	<b>115</b>
<b>Cash flows from investing activities:</b>		
Additions to property, plant, and equipment	(1,377)	(1,252)
Holdback payment related to the acquisition of Packaging Alternatives Corporation		(200)
<b>Net cash used in investing activities</b>	<b>(1,377)</b>	<b>(1,452)</b>
<b>Cash flows from financing activities:</b>		
Proceeds from the issuance of long-term debt		580
Principal repayments of long-term debt	(243)	(386)
Proceeds from exercise of stock options, net of attestation	81	31
Excess tax benefit on share-based compensation	563	
Payment of statutory withholdings for stock options exercised and restricted stock units vested	(701)	(426)
<b>Net cash used in financing activities</b>	<b>(300)</b>	<b>(201)</b>
Net decrease in cash and cash equivalents	(2,683)	(1,538)
<b>Cash and cash equivalents at beginning of period</b>	<b>37,303</b>	<b>33,480</b>
<b>Cash and cash equivalents at end of period</b>	<b>\$ 34,620</b>	<b>\$ 31,942</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, 2013, included in the Company's 2013 Annual Report on Form 10-K as filed with the Securities and Exchange Commission.

The condensed consolidated balance sheet as of March 31, 2014, the condensed consolidated statements of income for the three-month periods ended March 31, 2014 and 2013, and the condensed consolidated statements of cash flows for the three-month periods ended March 31, 2014 and 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, 2014, are not necessarily indicative of the results to be expected for the entire fiscal year ending December 31, 2014.

**(2) Supplemental Cash Flow Information**

Cash paid for interest and income taxes is as follows (in thousands):

	<b>Three Months Ended</b>			
	<b>March 31,</b>			
	<b>2014</b>		<b>2013</b>	
Interest	\$	31	\$	39
Income taxes, net of refunds	\$	80	\$	115

During the three-month periods ended March 31, 2014, and 2013, the Company permitted the exercise of stock options with exercise proceeds paid with the Company's stock (cashless exercises) totaling approximately \$203,000 and \$0, respectively.

**(3) Fair Value Accounting**

The Company has 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 fair value of the award and is recognized as an expense over the requisite service period (generally the vesting period of the equity grant).

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, 2013. The compensation cost charged against income for those plans is included in selling, general & administrative expenses as follows (in thousands):

## Edgar Filing: UFP TECHNOLOGIES INC - Form 10-Q

### Table of Contents

	<b>Three Months Ended</b>			
	<b>March 31,</b>			
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
Total share-based compensation expense	\$	265	\$	179

Share-based compensation for the three-month periods ended March 31, 2014, includes approximately \$5,000 representing the fair value of the Company's common stock granted during the quarter to a member of the Board of Directors.

The total income tax benefit recognized in the condensed consolidated statements of income for share-based compensation arrangements was approximately \$70,000 and \$55,000 for the three-month periods ended March 31, 2014 and 2013, respectively.

The following is a summary of stock option activity under all plans for the three-month period ended March 31, 2014:

	<b>Shares Under Options</b>	<b>Weighted Average Exercise Price (per share)</b>	<b>Weighted Average Remaining Contractual Life (in years)</b>	<b>Aggregate Intrinsic Value (in thousands)</b>
Outstanding at December 31, 2013	467,500	\$ 9.00		
Granted	577	25.48		
Exercised	(100,678)	2.82		
Cancelled or expired				
Outstanding at March 31, 2014	367,399	\$ 10.72	3.84	\$ 5,013
Exercisable at March 31, 2014	286,150	\$ 8.53	3.87	\$ 4,532
Vested and expected to vest at March 31, 2014	367,399	\$ 10.72	3.84	\$ 5,013

On March 12, 2014, the Company granted one of its directors, options to purchase 577 shares of its common stock at that day's closing price of \$25.48. The compensation expense related to this grant was determined as the fair value of the options using the Black Scholes option pricing model based on the following assumptions:

Expected volatility	38.0%
Expected dividends	none
Risk free interest rate	0.7%
Expected term	5.0 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, 2014 was \$8.67.

## Edgar Filing: UFP TECHNOLOGIES INC - Form 10-Q

During the three-month periods ended March 31, 2014 and 2013, 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 approximately \$2.3 million and \$100,000, respectively, and the total amount of consideration received by the Company from the exercised options was approximately \$284,000 and \$31,000, respectively. At its discretion, the Company allows option holders to surrender previously owned common stock in lieu of paying the exercise price and withholding taxes. During the three-months ended March 31, 2014, 25,094 shares (7,861 for options and 17,233 for taxes) were surrendered at an average market price of \$25.84.

## Edgar Filing: UFP TECHNOLOGIES INC - Form 10-Q

### Table of Contents

During the three-month periods ended March 31, 2014, and 2013, the Company recognized compensation expenses related to stock options granted to directors and employees of approximately \$94,000 and \$25,000, respectively.

On February 18, 2014, 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, 2014. The Company recorded compensation expense associated with the award of \$100,000 during the three-month period ended March 31, 2014. In the three-month period ended March 31, 2013, the Company recorded \$100,000 of compensation expense for a similar award.

The following table summarizes information about Restricted Stock Units ( RSUs ) activity during the three-month period ended March 31, 2014:

	<b>Restricted Stock Units</b>	<b>Weighted Average Award Date Fair Value</b>
Unvested at December 31, 2013	50,900	\$ 11.94
Awarded	21,660	25.97
Shares vested	(30,253)	10.11
Forfeited / cancelled		
Unvested at March 31, 2014	42,307	\$ 12.04

During the three-month periods ended March 31, 2014, and 2013, the Company recorded compensation expense related to RSUs of approximately \$66,000 and \$54,000, respectively.

At the Company's discretion, RSU holders are given the option to net-share settle to cover the required minimum withholding tax, and the remaining amount is converted into the equivalent number of common shares. During the three-months ended March 31, 2014; 9,878 shares were redeemed for this purpose at an average market price of \$25.88. During the three-months ended March 31, 2013, 22,089 shares were redeemed for this purpose at an average market price of \$19.29.

At March 31, 2014, the Company had approximately \$911,000 of unrecognized compensation expense which is expected to be recognized over a period of 4.0 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 (in thousands):

Edgar Filing: UFP TECHNOLOGIES INC - Form 10-Q

	March 31, 2014	December 31, 2013
Raw materials	\$ 7,635	\$ 6,627
Work in process	1,334	1,056
Finished goods	3,208	3,365
Total inventory	\$ 12,177	\$ 11,048

**(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.

Table of Contents**(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 number of common shares outstanding and dilutive common stock equivalent shares outstanding during each period.

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

	<b>Three Months Ended</b>	
	<b>March 31,</b>	
	<b>2014</b>	<b>2013</b>
Weighted average common shares outstanding, basic	6,972	6,768
Weighted average common equivalent shares due to stock options and RSUs	176	320
Weighted average common shares outstanding, diluted	7,148	7,088

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, 2014, and 2013, the number of stock awards excluded from the computation of diluted earnings per share for this reason was 577 and 64,337, respectively.

**(8) Segment Reporting**

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

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, 2013, 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 10% of the Company's consolidated revenues for the three-month period ended March 31, 2014. All of the Company's assets are located in the United States. Unallocated assets consist of the Company's cash balance. Financial statement information by reportable segment is as follows (in thousands):

Edgar Filing: UFP TECHNOLOGIES INC - Form 10-Q

	Three Months Ended March 31, 2014			Three Months Ended March 31, 2013		
	Component		Total	Component		Total
	Products	Packaging	UFPT	Products	Packaging	UFPT
	\$	\$	\$	\$	\$	\$
Net sales	23,611	10,998	34,609	23,417	10,280	33,697
Operating income	2,443	752	3,195	2,815	141	2,956
Depreciation / amortization	498	633	1,131	445	529	974
Capital expenditures	372	1,005	1,377	756	496	1,252



Table of Contents**(9) Other Intangible Assets**

The carrying values of the company's definite lived intangible assets as of March 31, 2014 and December 31, 2013, are as follows (in thousands):

	Patents	Non-Compete	Customer List	Total
Estimated useful life	14 years	5 years	5 years	
Gross amount at March 31, 2014	\$ 429	\$ 512	\$ 2,046	\$ 2,987
Accumulated amortization at March 31, 2014	(429)	(272)	(1,059)	(1,760)
Net balance at March 31, 2014	\$	\$ 240	\$ 987	\$ 1,227
Gross amount at December 31, 2013	\$ 429	\$ 512	\$ 2,046	\$ 2,987
Accumulated amortization at December 31, 2013	(429)	(249)	(963)	(1,641)
Net balance at December 31, 2013	\$	\$ 263	\$ 1,083	\$ 1,346

Amortization expense related to intangible assets was approximately \$119,000 and \$134,000 for the three-month periods ended March 31, 2014, and 2013, respectively. Future amortization as of March 31, 2014 will be approximately as follows (in thousands):

**Remainder of:**

2014	\$	273
2015		318
2016		318
2017		318
Total	\$	1,227

**(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 35.0% of income before income tax expense for the three-month period ended March 31, 2014, compared to a tax expense of approximately 30.4% for the comparable three-month period in 2013. The increase in the effective tax rate was a result of a retroactive application for a 2012 research and development credit which was recorded as a discrete event in the first quarter of 2013. Excluding this discrete event, the effective tax rate for the three months ended March 31, 2013, was also 35.0%.

**(11) Plant Consolidation**

On January 7, 2014, the Company committed to move forward with a plan to cease operations at its Glendale Heights, Illinois plant and consolidate operations into its Grand Rapids, Michigan facility. The Company's decision was in response to a pending significant increase in lease cost, declining sales at the Illinois facility, and significant anticipated savings as a result of the consolidation.

The Company expects to incur approximately \$1,150,000 in one-time expenses in connection with the consolidation, and to invest approximately \$300,000 in building improvements in Grand Rapids. Included in the \$1,150,000 amount above are approximately \$350,000 of expenses the Company expects to incur relating to employee severance payments, approximately \$550,000 in moving expenses and expenses associated with

Table of Contents

vacating the Glendale Heights building and approximately \$250,000 in expenses in moving equipment within the Grand Rapids location. Total cash charges are estimated at \$1,450,000. The Company expects annual cost savings of approximately \$750,000 as a result of the plant consolidation.

Through March 31, 2014, the Company has incurred approximately \$90,000 for workforce training, severance and other infrastructure costs related to the plant consolidation.

**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, expectations regarding the Company's results of operations, financial condition and the sufficiency of the Company's capital resources, statements regarding the Company's capital expenditure plans and expansion of our business and anticipated advantages associated there with including the development of and investments in its molded fiber product line, expectations regarding the manufacturing capacity and efficiencies of the Company's production equipment, anticipated advantages relating to the Company's decision to consolidate our Glendale Heights, Illinois facility into our Grand Rapids, Michigan facility and the expected costs, savings and efficiencies associated therewith, expected methods of growth for the Company, expectations regarding the Company's acquisition strategy, any indication that the Company may be able to sustain or increase its sales and earnings or sales and earnings growth rates and statements regarding 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. 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 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, 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.

## Edgar Filing: UFP TECHNOLOGIES INC - Form 10-Q

Unless the context requires otherwise, the terms we, us, our, or the Company refer to UFP Technologies, Inc. and its consolidated subsidiaries.

### Overview

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

The Company realized a 2.7% increase in year-to-date sales through March 31, 2014, compared to the same period in 2013, largely due to increases in sales to the automotive market, partially offset by sales declines in the military

Table of Contents

market. The Company was able to leverage this sales growth to generate an 8% increase in operating income for its first quarter.

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

**Results of Operations**

*Segment Results*

For the three-month period ended March 31, 2014, the sales and operating income for each of the Company's operating segments fluctuated as follows (in thousands):

	Sales			Operating Income		
	2014	March 31, 2013	Change	2014	March 31, 2013	Change
Component Products	\$ 23,611	\$ 23,417	\$ 194	\$ 2,443	\$ 2,815	\$ (372)
Packaging	10,998	10,280	718	752	141	611
Total	\$ 34,609	\$ 33,697	\$ 912	\$ 3,195	\$ 2,956	\$ 239

The increase in sales in the Component Products segment was primarily due to a 14% increase in sales to the automotive market, as discussed below. The decrease in operating income within the Component Products segment was primarily due to a shift in product mix as well as the absorption of approximately \$90,000 in costs associated with the consolidation of the Company's Illinois and Michigan plants.

The increase in sales in the Packaging segment was primarily due to a 16% increase in sales of molded fiber packaging, as discussed below. This sales increase was also the primary cause of the increase in Packaging segment operating income.

Further details regarding the Company's segment results of operations are described in Note 8 to the consolidated financial statements included in Part 1, Item 1 of this Quarterly Report on Form 10-Q.

*Sales*

Sales for the three-month period ended March 31, 2014 increased approximately 2.7% to \$34.6 million from sales of \$33.7 million for the same period in 2013. The increase in sales for the three-month period ended March 31, 2014, is primarily due to an increase of approximately \$800,000 in sales to the automotive market largely due to abnormally weak sales a year ago (Component Products segment) and an increase of approximately \$600,000 in sales of molded fiber packaging (Packaging segment) due to continued demand for environmentally friendly

## Edgar Filing: UFP TECHNOLOGIES INC - Form 10-Q

packaging and the Company's recent addition of production capacity. These increases were partially offset by a decline in sales to the military market of approximately \$500,000.

### *Gross Profit*

Gross profit as a percentage of sales ( gross margin ) decreased to 26.1% for the three-month period ended March 31, 2014, from 26.4% for the same period in 2013. The decrease in gross margin for the three-month period ended March 31, 2014 is primarily due to higher depreciation costs as well as costs incurred in connection with the Illinois plant consolidation (see Note 11 to the Interim Condensed Consolidated Financial Statements). As a percentage of sales, material and labor collectively declined 0.6% while overhead increased 1.1% (both the Component Products and Packaging segments).

### *Selling, General and Administrative Expenses*

Selling, general, and administrative expenses ( SG&A ) decreased approximately 1.9% to \$5.8 million for the three-month period ended March 31, 2014, from \$5.9 million for the same period in 2013. As a percentage of sales, SG&A decreased to 16.9% for the three-month period ended March 31, 2014, from 17.6% for the same three-month period in 2013. The decrease in SG&A as a percentage of sales for the three-month period ended March 31, 2014 is primarily due to the relatively fixed nature of SG&A expenses measured against higher sales.

Table of Contents

*Interest Expense*

The Company had net interest expense of approximately \$22,000 for the three-month period ended March 31, 2014, compared to net interest expense of approximately \$41,000 in the same period of 2013. The decrease in interest expense for the three-month period ended March 31, 2014, is primarily due to a lower average debt balance as a result of the Company's repayment of term loans in conjunction with the execution of a new revolving credit facility in the fourth quarter of 2013.

*Income Taxes*

The Company recorded a tax expense of approximately 35.0% of income before income tax expense for the three-month period ended March 31, 2014, compared to a tax expense of approximately 30.4% for the comparable three-month period in 2013. The increase in the effective tax rate was due to a retroactive application for a 2012 research and development credit which was recorded as a discrete event in the first quarter of 2013. Excluding this discrete event, the effective tax rate for the three months ended March 31, 2013 was 35.0%.

**Liquidity and Capital Resources**

The Company generally funds its operating expenses, capital requirements, and growth plan through internally generated cash and bank credit facilities. Working capital as of March 31, 2014 was \$57.9 million.

*Cash Flows*

Net cash used in operations for the three-month period ended March 31, 2014 was approximately \$1.0 million, primarily as a result of an increase in net receivables of approximately \$1.1 million driven by increased sales, an increase in inventory of approximately \$1.1 million primarily due to the timing of raw materials purchases, an increase in prepaid expenses of approximately \$1.4 million primarily due to the prepayment of insurance premiums and a decrease in accrued expenses of approximately \$2.5 million due to payments for 2013 year-end bonuses, annual profit sharing contributions and sales commissions. These cash outflows were partially offset by net income generated of approximately \$2.1 million, a reduction in refundable income taxes of approximately \$1.2 million and an increase in accounts payable of approximately \$1.6 million due to the timing of vendor payments in the ordinary course of business.

Net cash used in investing activities during the three-month period ended March 31, 2014, was approximately \$1.4 million and was primarily the result of additions of manufacturing machinery and equipment.

Net cash used in financing activities was approximately \$300,000 in the three-month period ended March 31, 2014, representing cash used to service term debt of approximately \$200,000 and to pay statutory withholding for stock options exercised and restricted stock units vested of

## Edgar Filing: UFP TECHNOLOGIES INC - Form 10-Q

approximately \$700,000, partially offset by excess tax benefits on share-based comp of approximately \$600,000.

### *Outstanding and Available Debt*

The Company maintains an unsecured \$40 million revolving credit facility with Bank of America, N.A. The credit facility calls for interest of LIBOR plus a margin that ranges from 1.0% to 1.5% or, at the discretion 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. Under the credit facility, the Company is subject to a minimum fixed-charge coverage financial covenant as well as a maximum total funded debt to EBITDA financial covenant. The Company's \$40 million credit facility matures on November 30, 2018.

As of March 31, 2014, the Company had no borrowings outstanding under the credit facility and the Company was in compliance with all covenants under the credit facility.

In 2012, the Company financed the purchase of two molded fiber machines through five-year term loans which mature in September 2017. The annual interest rate is fixed at 1.83% and the loans are secured by the related molded fiber machines. As of March 31, 2014, the outstanding balance of the term loans is approximately \$3.6 million.



Table of Contents

*Future Liquidity*

The Company requires cash to pay its operating expenses, purchase capital equipment, and to service its contractual obligations. The Company's principal sources of funds are its operations and its revolving credit facility. The Company used cash of approximately \$1.0 million in operations during the three-month period ended March 31, 2014 and cannot guarantee that its operations will generate cash in future periods. The Company expects its future cash flows from operations could be impacted by the state of the credit markets and the overall economy and the Company's production rates.

Throughout 2014, 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 expected to be 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**

There have been no material changes outside the ordinary course of business to our contractual obligations and commitments, as disclosed in our Annual Report on Form 10-K for the year ended December 31, 2013.

**Off-Balance-Sheet Arrangements**

The Company had no off-balance-sheet arrangements during the three-month period ended March 31, 2014, other than operating leases.

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

There have been no material changes in our market risks as previously disclosed in Item 7A of our Annual Report on Form 10-K for the year ended December 31, 2013.

**ITEM 4: CONTROLS AND PROCEDURES**

## Edgar Filing: UFP TECHNOLOGIES INC - Form 10-Q

As of the end of the period covered by this report (the Evaluation Date ), the Company's management, under the supervision and with the participation of the Company's Chief Executive Officer and Chief Financial Officer, performed an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in SEC Rule 13a-15(e) or 15d-15(e)). Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of the Evaluation Date, 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, as amended, is (i) recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and (ii) accumulated and communicated to the Company's management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

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.

Table of Contents

**PART II: OTHER INFORMATION**

**ITEM 1A: 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, 2013.

**ITEM 6: EXHIBITS**

<b>Exhibit No.</b>	<b>Description</b>
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.*
32.1	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.*

---

\* Filed herewith.

\*\* Furnished herewith.

Table of Contents

**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 12, 2014

By: /s/ R. Jeffrey Bailly  
R. Jeffrey Bailly  
Chairman, Chief Executive Officer,  
President, and Director  
(Principal Executive Officer)

Date: May 12, 2014

By: /s/ Ronald J. Lataille  
Ronald J. Lataille  
Chief Financial Officer  
(Principal Financial Officer)

**EXHIBIT INDEX**

<b>Exhibit No.</b>	<b>Description</b>
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.*
32.1	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.*

---

\* Filed herewith.

\*\* Furnished herewith.