

PHOTRONICS INC
Form 10-Q
March 07, 2012

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 January 29, 2012
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 0-15451

PHOTRONICS, INC.
(Exact name of registrant as specified in its charter)

Connecticut 06-0854886
(State or other jurisdiction of incorporation or (IRS Employer Identification No.)
organization)

15 Secor Road, Brookfield, Connecticut 06804
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code (203) 775-9000

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 periods 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 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 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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

| Class | Outstanding at March 1, 2012 |
|--------------------------------|------------------------------|
| Common Stock, \$0.01 par value | 60,384,433 Shares |

Forward-Looking Statements

The Private Securities Litigation Reform Act of 1995 provides a "safe harbor" for forward-looking statements made by or on behalf of Photronics, Inc. ("Photronics" or the "Company"). These statements are based on management's beliefs, as well as assumptions made by, and information currently available to, management. Forward-looking statements may be identified by words like "expect", "anticipate", "believe", "plan", "projects", and similar expressions, or the negative of such terms, or other comparable terminology. All forward-looking statements involve risks and uncertainties that are difficult to predict. In particular, any statement contained in this quarterly report on Form 10-Q, in press releases, written statements, or other documents filed with the Securities and Exchange Commission, or in the Company's communications and discussions with investors and analysts in the normal course of business through meetings, phone calls, or conference calls regarding the consummation and benefits of future acquisitions, expectations with respect to future sales, financial performance, operating efficiencies, or product expansion, are subject to known and unknown risks, uncertainties, and contingencies, many of which are beyond the control of the Company. These factors may cause actual results, performance, or achievements to differ materially from anticipated results, performance, or achievements expressed or implied by such forward-looking statements. Factors that might affect such forward-looking statements include, but are not limited to, overall economic and business conditions; economic and political conditions in international markets; the demand for the Company's products; competitive factors in the industries and geographic markets in which the Company competes; changes in federal, state and international tax requirements (including tax rate changes, new tax laws and revised tax law interpretations); interest rate fluctuations and other capital market conditions, including changes in the market price of the Company's common stock; foreign currency exchange rate fluctuations; changes in technology; the timing, impact, and other uncertainties of future acquisitions; the seasonal and cyclical nature of the semiconductor and flat panel display industries; management changes; damage or destruction to the Company's facilities, or the facilities of its customers or suppliers, by natural disasters, labor strikes, political unrest, or terrorist activity; the ability of the Company to (i) place new equipment in service on a timely basis; (ii) obtain additional financing; (iii) achieve anticipated synergies and other cost savings in connection with acquisitions and productivity programs; (iv) fully utilize its tools; (v) achieve desired yields, pricing, product mix, and market acceptance of its products and (vi) obtain necessary export licenses. Any forward-looking statements should be considered in light of these factors. Accordingly, there is no assurance that the Company's expectations will be realized. The Company does not assume responsibility for the accuracy and completeness of the forward-looking statements and does not assume an obligation to provide revisions to any forward-looking statements, except as otherwise required by securities and other applicable laws.

PHOTRONICS, INC.
AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION

Item 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

PHOTRONICS, INC. AND SUBSIDIARIES
Condensed Consolidated Balance Sheets
(in thousands, except per share amounts)
(unaudited)

| | January 29, 2012 | October 30, 2011 |
|--|---------------------|---------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$201,800 | \$189,928 |
| Accounts receivable, net of allowance of \$3,890 in 2012 and \$4,055 in 2011 | 84,092 | 85,540 |
| Inventories | 21,626 | 22,100 |
| Deferred income taxes | 622 | 609 |
| Other current assets | 7,515 | 7,030 |
| Total current assets | 315,655 | 305,207 |
| Property, plant and equipment, net | 359,814 | 368,680 |
| Investment in joint venture | 80,365 | 79,984 |
| Intangible assets, net | 41,194 | 42,462 |
| Deferred income taxes | 11,285 | 11,239 |
| Other assets | 11,378 | 10,282 |
| Total assets | \$819,691 | \$817,854 |
| LIABILITIES AND EQUITY | | |
| Current liabilities: | | |
| Current portion of long-term borrowings | \$5,529 | \$5,583 |
| Accounts payable | 54,140 | 54,772 |
| Accrued liabilities | 35,498 | 35,546 |
| Total current liabilities | 95,167 | 95,901 |
| Long-term borrowings | 151,257 | 152,577 |
| Deferred income taxes | 736 | 737 |
| Other liabilities | 8,085 | 8,883 |
| Total liabilities | 255,245 | 258,098 |
| Commitments and contingencies | | |
| Equity: | | |
| Preferred stock, \$0.01 par value, 2,000 shares authorized, none issued and outstanding | - | - |
| Common stock, \$0.01 par value, 150,000 shares authorized, 60,015 shares issued and outstanding at January 29, 2012 and 59,651 at October 30, 2011 | 600 | 597 |
| Additional paid-in capital | 488,674 | 486,674 |

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| | | |
|---|-----------|-----------|
| Retained earnings | 17,873 | 13,605 |
| Accumulated other comprehensive income | 8,773 | 10,171 |
| Total Photronics, Inc. shareholders' equity | 515,920 | 511,047 |
| Noncontrolling interests | 48,526 | 48,709 |
| Total equity | 564,446 | 559,756 |
| Total liabilities and equity | \$819,691 | \$817,854 |

See accompanying notes to condensed consolidated financial statements.

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PHOTRONICS, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Income
(in thousands, except per share amounts)
(unaudited)

| | Three Months Ended | |
|---|---------------------|---------------------|
| | January 29, 2012 | January 30, 2011 |
| Net sales | \$112,154 | \$120,823 |
| Costs and expenses: | | |
| Cost of sales | (86,696) | (90,229) |
| Selling, general and administrative | (11,325) | (10,713) |
| Research and development | (4,444) | (3,771) |
| Consolidation, restructuring and related charges | (1,118) | - |
| Operating income | 8,571 | 16,110 |
| Other income (expense): | | |
| Interest expense | (1,781) | (1,711) |
| Investment and other income, net | 1,372 | 2,668 |
| Income before income taxes | 8,162 | 17,067 |
| Income tax provision | (3,321) | (3,483) |
| Net income | 4,841 | 13,584 |
| Net income attributable to noncontrolling interests | (573) | (1,473) |
| Net income attributable to Photronics, Inc. | \$4,268 | \$12,111 |
| Earnings per share: | | |
| Basic | \$0.07 | \$0.23 |
| Diluted | \$0.07 | \$0.20 |
| Weighted-average number of common shares outstanding: | | |
| Basic | 59,817 | 53,817 |
| Diluted | 60,930 | 66,411 |

See accompanying notes to condensed consolidated financial statements.

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PHOTRONICS, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows
(in thousands)
(unaudited)

| | Three Months Ended | |
|---|---------------------|---------------------|
| | January 29, 2012 | January 30, 2011 |
| Cash flows from operating activities: | | |
| Net income | \$4,841 | \$13,584 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 22,667 | 23,189 |
| Consolidation, restructuring and related charges | 232 | - |
| Changes in assets and liabilities: | | |
| Accounts receivable | 1,287 | 4,139 |
| Inventories | 383 | (5,299) |
| Other current assets | (542) | 360 |
| Accounts payable, accrued liabilities, and other | 5,167 | 5,682 |
| Net cash provided by operating activities | 34,035 | 41,655 |
| Cash flows from investing activities: | | |
| Purchases of property, plant and equipment | (18,127) | (19,120) |
| Investment in joint venture | (400) | (3,999) |
| Other | (1,602) | - |
| Net cash used in investing activities | (20,129) | (23,119) |
| Cash flows from financing activities: | | |
| Repayments of long-term borrowings | (999) | (24,346) |
| Repurchase of common stock by subsidiary | (885) | - |
| Proceeds from share-based payments | 233 | 159 |
| Proceeds from long-term borrowings | - | 17,000 |
| Net cash used in financing activities | (1,651) | (7,187) |
| Effect of exchange rate changes on cash | (383) | 2,429 |
| Net increase in cash and cash equivalents | 11,872 | 13,778 |
| Cash and cash equivalents at beginning of period | 189,928 | 98,945 |
| Cash and cash equivalents at end of period | \$201,800 | \$112,723 |
| Supplemental disclosure of cash flow information: | | |
| Change in accrual for purchases of property, plant and equipment | \$ 5,159 | \$ 13,273 |

See accompanying notes to condensed consolidated financial statements.

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PHOTRONICS, INC. AND SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements
Three Months Ended January 29, 2012 and January 30, 2011
(unaudited)
(in thousands, except share amounts)

NOTE 1 - BASIS OF FINANCIAL STATEMENT PRESENTATION

Photronics, Inc. and its subsidiaries ("Photronics" or "the Company") is one of the world's leading manufacturers of photomasks, which are high precision photographic quartz plates containing microscopic images of electronic circuits. Photomasks are a key element in the manufacture of semiconductors and flat panel displays ("FPDs"), and are used as masters to transfer circuit patterns onto semiconductor wafers and flat panel substrates during the fabrication of integrated circuits ("ICs") and a variety of FPDs and, to a lesser extent, other types of electrical and optical components. The Company currently operates principally from eight manufacturing facilities, two of which are located in Europe, two in Taiwan, one in Korea, and three in the United States. The Company ceased manufacturing photomasks at its Singapore facility in December 2011.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for annual financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. Operating results for the interim period are not necessarily indicative of the results that may be expected for the fiscal year ending October 28, 2012. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended October 30, 2011.

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NOTE 2 - CHANGES IN EQUITY AND COMPREHENSIVE INCOME

The following tables set forth the Company's consolidated changes in equity and comprehensive income (net of tax of \$0) for the three months ended January 29, 2012 and January 30, 2011:

| | Three Months Ended January 29, 2012 | | | | | | | |
|---|-------------------------------------|------------------------|-----------------------------|----------------------|---|------------------------------|----------------------------------|-----------------|
| | Photronics, Inc. Shareholders | | | | | | | |
| | Common Stock Shares | Common Stock Amount | Add'l Paid-in Capital | Retained Earnings | Accum- ulated Other Compre- hensive Income | Total Photronics, Inc. | Non- controlling Interests | Total Equity |
| Balance at October 31, 2011 | 59,651 | \$597 | \$486,674 | \$13,605 | \$10,171 | \$511,047 | \$48,709 | \$559,756 |
| Comprehensive income: | | | | | | | | |
| Net income | - | - | - | 4,268 | - | 4,268 | 573 | 4,841 |
| Amortization of cash flow hedges | - | - | - | - | 32 | 32 | - | 32 |
| Foreign currency translation adjustments | - | - | - | - | (1,425) | (1,425) | 275 | (1,150) |
| Total comprehensive income | | | | | | 2,875 | 848 | 3,723 |
| Sale of common stock through employee stock option and purchase plans | 122 | 1 | 143 | - | - | 144 | - | 144 |
| Restricted stock awards vesting and expense | 65 | - | 242 | - | - | 242 | - | 242 |
| Share-based compensation expense | - | - | 413 | - | - | 413 | - | 413 |
| Common stock warrants exercised | 177 | 2 | 1,051 | - | - | 1,053 | - | 1,053 |
| Repurchase of common stock by subsidiary | - | - | 151 | - | (5) | 146 | (1,031) | (885) |
| Balance at January 29, 2012 | 60,015 | \$600 | \$488,674 | \$17,873 | \$8,773 | \$515,920 | \$48,526 | \$564,446 |

Three Months Ended January 30, 2011
Photronics, Inc. Shareholders

| Common Stock | Add'l | (Accum- ulated Deficit) | Accum- ulated Other Compre- | Total | Non- |
|--------------|-------|-------------------------------|--------------------------------------|-------|------|
|--------------|-------|-------------------------------|--------------------------------------|-------|------|

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| | Shares | Amount | Paid-in Capital | Retained Earnings | hensive Income | Photronics, Inc. | controlling Interests | Total Equity |
|---|--------|--------|--------------------|----------------------|-------------------|------------------|--------------------------|-----------------|
| Balance at November 1, 2010 | 53,779 | \$538 | \$436,825 | \$(2,624) | \$7,062 | \$ 441,801 | \$ 54,142 | \$495,943 |
| Comprehensive income: | | | | | | | | |
| Net income | - | - | - | 12,111 | - | 12,111 | 1,473 | 13,584 |
| Amortization of cash flow hedges | - | - | - | - | 32 | 32 | - | 32 |
| Foreign currency translation adjustments | - | - | - | - | 5,812 | 5,812 | 2,555 | 8,367 |
| Total comprehensive income | | | | | | 17,955 | 4,028 | 21,983 |
| Sale of common stock through employee stock option and purchase plans | 65 | 1 | 58 | - | - | 59 | - | 59 |
| Restricted stock awards vesting and expense | 21 | - | 188 | - | - | 188 | - | 188 |
| Share-based compensation expense | - | - | 289 | - | - | 289 | - | 289 |
| Balance at January 30, 2011 | 53,865 | \$539 | \$437,360 | \$9,487 | \$12,906 | \$ 460,292 | \$ 58,170 | \$518,462 |

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NOTE 3 - JOINT VENTURE, TECHNOLOGY LICENSE AND OTHER AGREEMENTS WITH MICRON TECHNOLOGY, INC.

On May 5, 2006, Photronics and Micron Technology, Inc. ("Micron") entered into the MP Mask joint venture ("MP Mask"), which develops and produces photomasks for leading-edge and advanced next generation semiconductors. As part of the formation of the joint venture, Micron contributed its existing photomask technology center located in Boise, Idaho, (headquarters of MP Mask) and Photronics invested \$135 million in exchange for a 49.99% interest in MP Mask (to which \$64.2 million of the original investment was allocated), a license for photomask technology of Micron, and certain supply agreements.

This joint venture is a variable interest entity ("VIE") (as that term is defined in the Accounting Standards Codification ("ASC")) because all costs of the joint venture are passed on to the Company and Micron through purchase agreements they have entered into with the joint venture, and it is dependent upon the Company and Micron for any additional cash requirements. On a quarterly basis the Company reassesses whether its interest in MP Mask gives it a controlling financial interest in this VIE. The purpose of this quarterly reassessment is to identify the primary beneficiary (which is defined in the ASC as the entity that consolidates a VIE) of the VIE. As a result of the reassessment in the current quarter, the Company determined that Micron is still the primary beneficiary of the VIE, by virtue of its tie-breaking voting rights within MP Mask's Board of Managers, thereby giving it the power to direct the activities of MP Mask that most significantly impact its economic performance, including its decision making authority in the ordinary course of business and its purchasing the majority of products produced by the VIE.

The Company has utilized MP Mask for both high-end IC photomask production and research and development purposes. MP Mask charges its variable interest holders based on their actual usage of its facility. MP Mask separately charges for any research and development activities it engages in at the requests of its owners. The Company recorded cost of sales of \$2.0 million and \$3.5 million during the three month periods ended January 29, 2012 and January 30, 2011, respectively, and research and development expenses of \$0.2 million during each of the three month periods.

MP Mask is governed by a Board of Managers, appointed by Micron and the Company. Since MP Mask's inception, Micron, as a result of its majority ownership, has held majority voting power on the Board of Managers. The voting power held by each party is subject to change as ownership interests change. Under the MP Mask joint venture operating agreement, the Company may be required to make additional capital contributions to MP Mask up to the maximum amount defined in the operating agreement. However, should the Board of Managers determine that further additional funding is required, MP Mask shall pursue its own financing. If MP Mask is unable to obtain its own financing, it may request additional capital contributions from the Company. Should the Company choose not to make a requested contribution to MP Mask, its ownership percentage may be reduced. The Company made additional capital contributions to the MP Mask joint venture of \$0.4 million and \$4.0 million during the three month periods ending January 29, 2012 and January 30, 2011, respectively, which were primarily related to capital calls made by the joint venture. In March 2012 the Company made an additional capital contribution to MP Mask of \$5.5 million. The Company did not receive any distributions from MP Mask during the first quarter of fiscal 2012 or 2011.

The Company's investment in the VIE, which represents its maximum exposure to loss, was \$80.4 million at January 29, 2012 and \$80.0 million at October 30, 2011. These amounts are reported in the Company's condensed consolidated balance sheets as "Investment in joint venture". The Company recorded income from its investment in the VIE of \$0.7 million in the three month period ended January 30, 2011, and recorded no income from its investment in the three month period ended January 29, 2012. Income from the VIE is included in "Investment and other income, net" in the condensed consolidated statements of income.

In the first quarter of 2008 a capital lease agreement with Micron commenced for the U.S. nanoFab facility. Quarterly lease payments, which bore interest at 8%, were \$3.8 million through January 2013. This lease was

cancelled in the third fiscal quarter of 2009, at which time the Company and Micron (the lessor) entered into a new lease agreement for the facility. Under the provisions of the new lease agreement, quarterly lease payments were reduced from \$3.8 million to \$2.0 million, the term of the lease was extended from December 31, 2012 to December 31, 2014, and ownership of the property would not transfer to the Company at the end of the lease term. The interest rate of the new lease agreement remained at 8%. As a result of the new lease agreement, the Company reduced its lease obligation and the carrying value of its assets under capital leases by approximately \$28 million. The Company paid the capital lease obligation in full in April 2011 with a portion of the net proceeds of the March 2011 issuance of its 3.25% convertible senior notes.

In the second quarter of fiscal 2012 the Company paid \$35 million to Micron in connection with the purchase of the U.S. nanoFab facility and the remaining term of the operating lease agreement through 2014 was cancelled. Also in connection with this purchase, the Company entered into a \$25 million term loan agreement in the second quarter of fiscal 2012 (see Notes 4 and 14 for further discussion).

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NOTE 4 - LONG-TERM BORROWINGS

Long-term borrowings consist of the following:

| | January 29, 2012 | October 30, 2011 |
|---|---------------------|---------------------|
| 3.25% convertible senior notes due on April 1, 2016 | \$ 115,000 | \$ 115,000 |
| 5.50% convertible senior notes due on October 1, 2014 | 22,054 | 22,054 |
| 3.09% capital lease obligation payable through March 2016 | 18,219 | 19,218 |
| 4.75% financing loan with customer | 1,513 | 1,888 |
| | 156,786 | 158,160 |
| Less current portion | 5,529 | 5,583 |
| | \$ 151,257 | \$ 152,577 |

In March 2011 the Company issued through a private offering, pursuant to Rule 144A under the Securities Act of 1933, as amended, \$115 million aggregate principal amount of 3.25% convertible senior notes. The notes mature on April 1, 2016, and note holders may convert each \$1,000 principal amount of notes to 96.3879 shares of common stock (equivalent to an initial conversion price of \$10.37 per share of common stock) at any time prior to the close of business on the second scheduled trading day immediately preceding April 1, 2016. The conversion rate is subject to adjustment upon the occurrence of certain events, which are described in the indenture dated March 28, 2011. The Company is not required to redeem the notes prior to their maturity date. Interest on the notes accrues in arrears, and is paid semiannually through the notes' maturity date. Interest payments on the notes commenced on October 1, 2011. The net proceeds of the notes were approximately \$110.7 million, which were used, in part, to acquire \$35.4 million of the Company's 5.5% convertible senior notes which were to mature on October 1, 2014, and to repay, in full, its then outstanding obligations under capital leases of \$19.8 million.

In June 2011 the Company acquired \$5.0 million of its 5.5% convertible senior notes in exchange for 0.7 million shares of its common stock, with a fair value of \$6.5 million, and cash of \$3.2 million (the note holders received 147.529 shares and cash of \$647 for each \$1,000 note). The Company, in connection with this repurchase, recorded an extinguishment loss of \$5.0 million, which included the write off of deferred financing fees of \$0.3 million.

In March 2011 the Company acquired \$30.4 million of its 5.5% convertible senior notes in exchange for 4.5 million shares of its common stock, with a fair value of \$39.2 million, and cash of \$19.7 million (the note holders received 147.529 shares and cash of \$647 for each \$1,000 note). The Company, in connection with this repurchase, recorded an extinguishment loss of \$30.1 million, which included the write off of deferred financing fees of \$1.7 million.

In September 2009 the Company issued, through a public offering, \$57.5 million aggregate principal amount of 5.5% convertible senior notes, which were to mature on October 1, 2014. Under the terms of the offering, the note holders could convert each \$1,000 principal amount of notes to 196.7052 shares of common stock (equivalent to an initial conversion price of \$5.08 per share of common stock) on, or before, September 30, 2014. The conversion rate is subject to adjustment upon the occurrence of certain events which are described in the indenture dated September

16, 2009. The Company is not required to redeem the notes prior to their maturity. The net proceeds of this offering were approximately \$54.9 million, which were used to reduce amounts outstanding under the Company's credit facility. As discussed above, \$35.4 million aggregate principal amount of these notes were acquired by the Company during fiscal year 2011.

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In April 2011 the Company entered into a five year, \$21.2 million capital lease for manufacturing equipment. Payments under the lease, which bears interest at 3.09%, are \$0.4 million per month through March 2016. The lease agreement provides that the Company must maintain the equipment in good working order, and includes a cross default with cross acceleration provision related to certain non-financial covenants incorporated in the Company's credit facility agreement. As of January 29, 2012, the total amount payable through the end of the lease term was \$19.5 million, of which \$18.2 million represented principal and \$1.3 million represented interest.

In January 2010 the Company borrowed \$3.7 million from a customer to purchase manufacturing equipment. This loan bears interest at 4.75% and is primarily being repaid with product supplied to the customer. Product valued at \$0.3 million was shipped to the customer and applied against the loan during both the first quarters of fiscal 2012 and fiscal 2011. The Company estimates that the loan will be fully repaid in fiscal 2013.

In March 2011 the Company amended its revolving credit facility ("the credit facility") which, as amended, included, among other things: i) a reduction of the aggregate commitments of the lenders from \$65 million to \$30 million; ii) a reduction of the applicable interest rates and modifications of the leverage ratios related thereto; iii) an extension of the maturity date to April 30, 2015; iv) an increase in the permitted amount of certain financed capital assets up to \$75 million outstanding at any one time; v) an allowance to issue the 3.25% convertible senior notes; vi) an increase in the investments "basket" from \$15 million to \$25 million per year; vii) an allowance to repurchase the 5.5% convertible senior notes and other indebtedness; and viii) removal of the limitation on maximum last twelve months capital expenditures. The credit facility bears interest (2.5% at January 29, 2012), based on the Company's total leverage ratio, at LIBOR plus a spread, as defined in the credit facility.

In the second quarter of fiscal 2012 the Company, in connection with its purchase of the U.S. nanoFab facility (see Notes 3 and 14 for further discussion), amended the credit facility. The amendment included the addition of a \$25 million term loan maturing in March 2017 with quarterly principal payments of \$0.6 million (quarterly payments are based on a ten year repayment period commencing in June 2012). The amendment also included a twenty-five basis point reduction in the interest rate charged on any borrowings under the credit facility.

The credit facility is secured by substantially all of the Company's assets located in the United States, as well as common stock the Company owns in certain of its foreign subsidiaries, and is subject to the following financial covenants: minimum fixed charge ratio, total leverage ratio and minimum unrestricted cash balance. As of January 29, 2012, the Company had no outstanding borrowings under the credit facility and \$30 million was available for borrowing.

NOTE 5 - COMMON STOCK WARRANTS

In September 2009 the Company entered into two warrant agreements with Intel Capital Corporation to purchase a total of 750,000 shares of the Company's common stock. Under one warrant agreement 500,000 shares of the Company's common stock can be purchased at an exercise price of \$4.15 per share and under the second warrant agreement 250,000 shares of the Company's common stock can be purchased at an exercise price of \$5.08 per share. The warrant agreements expire in September 2014. Also in September 2009, the Company and Intel Corporation entered into an agreement to share technical and operations information regarding the development of the Company's products, the capabilities of the Company's photomask manufacturing lines and the alignment of photomask toolsets. Intel Capital Corporation also invested in the Company's convertible debt offering of September 2009. The warrants were recorded at their fair value on their date of grant, which was determined using the Black-Scholes option pricing model. As of January 29, 2012, none of the warrants issued to Intel Capital Corporation had been exercised.

In conjunction with the May 2009 amendment to its then existing credit facility, the Company also entered into a warrant agreement with its lenders. See Note 6 for further discussion of these warrants.

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NOTE 6 - DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

The Company utilizes derivative instruments to reduce its exposure to the effects of the variability of interest rates and foreign currencies on its financial performance when it believes such action is warranted. Historically, the Company has been a party to derivative instruments to hedge either the variability of cash flows of a prospective transaction or the fair value of a recorded asset or liability. In certain instances, the Company has designated these transactions as hedging instruments. However, whether or not a derivative was designated as being a hedging instrument, the Company's purpose for engaging in the derivative has always been for risk management (and not speculative) purposes. The Company historically has not been a party to a significant number of derivative instruments and does not expect its derivative activity to significantly increase in the foreseeable future.

In addition to the utilization of derivative instruments discussed above, the Company attempts to minimize its risk of foreign currency exchange rate variability by, whenever possible, procuring production materials within the same country that it will utilize the materials in manufacturing, and by selling to customers from manufacturing sites within the country in which the customers are located.

In May 2009, in connection with an amendment to its credit facility, the Company issued 2.1 million warrants, each exercisable for one share of the Company's common stock at an exercise price of \$0.01 per share. Forty percent of the warrants were exercisable upon issuance, and the remaining balance was to become exercisable in twenty percent increments at various points in time after October 31, 2009. As a result of certain net cash settleable put provisions within the warrant agreement, the warrants were recorded as a liability in the Company's consolidated balance sheet. As of the issuance date and for future periods that such warrants remained outstanding, the Company had adjusted the liability based upon the current fair value of the warrants, with any changes in their fair value being recognized in earnings. Due to the warrants' exercise price of \$0.01 per share, their fair value approximated the market price of the Company's common stock. Approximately 1.2 million of these warrants were cancelled as a result of the Company's early repayment of certain amounts under its credit facility during the year ended November 1, 2009, and the associated liability was reduced accordingly. During the three month period ended January 29, 2012, all of the 0.2 million of these warrants that remained outstanding were exercised. In connection with this exercise, the Company recognized a gain of \$0.1 million, included in investment and other income, net, in its condensed consolidated statements of income. During the comparable period in 2011, 0.1 million of these warrants were exercised, which resulted in the Company recognizing a charge in the amount of \$0.1 million, and was also included in investment and other income, net.

A portion of an existing loss on a cash flow hedge in the amount of \$0.1 million is expected to be reclassified into earnings over the next twelve months.

The table below presents the effect of derivative instruments on the Company's condensed consolidated balance sheets at January 29, 2012 and October 30, 2011.

| Derivatives Not Designated as Hedging Instruments Under ASC 815 | Balance Sheet Location | Fair Value at | |
|---|------------------------|---------------------|---------------------|
| | | January 29, 2012 | October 30, 2011 |
| Warrants on common stock | Other liabilities | \$ - | \$ 1,147 |

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The table below presents the effect of derivative instruments on the Company's condensed consolidated statements of income for the three month periods ended January 29, 2012 and January 30, 2011.

| Derivatives Not Designated as Hedging Instruments Under ASC 815 | Location of Gain (Loss) Related to Derivative Instruments | Amount of Gain (Loss) Recognized Related to Derivative Instruments | |
|---|--|---|---------------------|
| | | Three Months Ended | |
| | | January 29, 2012 | January 30, 2011 |
| Warrants on common stock | Investment and other income (expense), net | \$ 94 | \$ (75) |

NOTE 7 - SHARE-BASED COMPENSATION

In March 2007 shareholders approved a new share-based compensation plan ("Plan"), under which options, restricted stock, restricted stock units, stock appreciation rights, performance stock, performance units, and other awards based on, or related to, shares of the Company's common stock may be granted from shares authorized but unissued or shares previously issued and reacquired by the Company. Currently, a maximum of six million shares of common stock may be issued under the Plan. Awards may be granted to officers, employees, directors, consultants, advisors, and independent contractors of the Company or its subsidiaries. In the event of a change in control (as defined in the Plan), the vesting of awards may be accelerated. The Plan, aspects of which are more fully described below, prohibits further awards from being issued under prior plans. The Company incurred total share-based compensation costs of \$0.7 million and \$0.5 million for the three month periods ended January 29, 2012 and January 30, 2011, respectively. No share-based compensation cost was capitalized as part of an asset and no related income tax benefits were recorded during the periods presented.

Stock Options

Option awards generally vest in one to four years, and have a ten-year contractual term. All incentive and non-qualified stock option grants have an exercise price no less than the market value of the underlying common stock on the date of grant. The grant date fair values of options are based on closing prices of the Company's common stock on the dates of grant using the Black-Scholes option pricing model. Expected volatility is based on the historical volatility of the Company's stock. The Company uses historical option exercise behavior and employee termination data to estimate expected term, which represents the period of time that the options granted are expected to remain outstanding. The risk-free rate of return for the estimated term of the option is based on the U.S. Treasury yield curve in effect at the date of grant. The weighted-average inputs and risk-free rate of return ranges used to calculate the grant date fair value of options issued during the three month periods ended January 29, 2012 and January 30, 2011, are presented in the following table.

| | Three Months Ended | |
|--------------------------|---------------------|---------------------|
| | January 29, 2012 | January 30, 2011 |
| Volatility | 102.1% | 98.6% |
| Risk free rate of return | 0.7% | 1.0% - 1.6% |

| | | |
|----------------|-----------|-----------|
| Dividend yield | 0.0% | 0.0% |
| Expected term | 4.3 years | 4.2 years |

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Information on outstanding and exercisable option awards as of January 29, 2012, is presented below.

| Options | Shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Life | Aggregate Intrinsic Value |
|---------------------------------|-----------|--|---|---------------------------------|
| Outstanding at January 29, 2012 | 4,168,014 | \$ 8.30 | 6.6 years | \$ 8,894 |
| Exercisable at January 29, 2012 | 2,322,192 | \$ 10.98 | 5.1 years | \$ 4,530 |

There were 492,500 share options granted during the three month period ended January 29, 2012, with a weighted-average grant date fair value of \$4.46 per share, and there were 251,500 share options granted during the three month period ended January 30, 2011, with a weighted-average grant date fair value of \$4.67 per share. As of January 29, 2012, the total unrecognized compensation cost related to unvested option awards was approximately \$4.3 million. That cost is expected to be recognized over a weighted-average amortization period of 2.9 years.

Restricted Stock

The Company periodically grants restricted stock awards. The restrictions on these awards lapse over a service period that has ranged from less-than-one to eight years. There were 168,750 restricted stock awards issued during the three month period ended January 29, 2012, with a weighted-average grant date fair value of \$6.28 per share, and there were 176,250 restricted stock awards granted during the three month period ended January 30, 2011, with a weighted-average grant date fair value of \$6.71 per share. As of January 29, 2012, the total compensation cost not yet recognized related to unvested restricted stock awards was approximately \$1.8 million. That cost is expected to be recognized over a weighted-average amortization period of 2.7 years. As of January 29, 2012, there were 295,377 shares of restricted stock outstanding.

NOTE 8 - CONSOLIDATION, RESTRUCTURING AND RELATED CHARGES

In the first quarter of fiscal 2012 the Company ceased the manufacture of photomasks at its Singapore facility, and in connection therewith recorded a charge of \$1.1 million during the three month period ended January 29, 2012. The Company expects that this restructuring will be completed in fiscal 2012, and expects its total cost to range between \$1.5 million and \$1.9 million, with that cost primarily being comprised of employee termination costs and asset write-downs. The following table sets forth the Company's restructuring reserve primarily related to its Singapore facility as of January 29, 2012, and reflects the activity affecting the reserve for the three month period then ended.

| | October 31, 2011 | Three Months Ended January 29, 2012 | | January 29, 2012 |
|---------------------------------|---------------------|--|-----------|---------------------|
| | | Charges | Utilized | |
| Employee terminations and other | \$ - | \$ 886 | \$ (467) | \$ 419 |
| Asset write-downs | - | 232 | (232) | - |
| | \$ - | \$ 1,118 | \$ (699) | \$ 419 |

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NOTE 9 - INCOME TAXES

The effective income tax rates differ from the rates computed by applying the U.S. statutory rate of 35% to income before income taxes in the first quarters of fiscal 2012 and 2011, primarily due to a higher level of earnings being taxed at lower statutory rates in foreign jurisdictions. In the first quarter of 2012, the impact of the lower statutory rates was offset as, due to valuation allowances, no income tax benefit was recognized in jurisdictions in which the Company incurred losses before income taxes. Further, in fiscal 2012 and 2011 in Korea, and in fiscal 2011 at PSMC in Taiwan, various investment tax credits have been earned which also reduced the Company's effective income tax rate in that year.

The Company accounts for uncertain tax positions by recording a liability for unrecognized tax benefits resulting from uncertain tax positions taken, or expected to be taken, in its tax returns. The Company recognizes any interest and penalties related to uncertain tax positions in the income tax provision in its condensed consolidated statements of income.

Unrecognized tax benefits associated with uncertain tax positions of \$2.0 million and \$1.9 million are included in the condensed consolidated balance sheets at January 29, 2012 and October 30, 2011, respectively, of which, at both dates, \$0.5 million is included in accrued liabilities, and the balances are included in other liabilities. Included in these amounts were \$0.1 million for interest and penalties in the two periods. If recognized, the benefits would favorably affect the Company's effective income tax rate in future periods. As of January 29, 2012, the Company believes it is not reasonably possible that the total amounts of unrecognized tax benefits will significantly increase or decrease in the next twelve months. Currently, the statutes of limitations remain open subsequent to, and including, 2008 in the U.S., 2009 in the U.K., 2008 in Germany, 2011 in Korea, 2010 in Taiwan and 2006 in Singapore.

PKLT, the Company's FPD manufacturing facility in Taiwan, is accorded a tax holiday which commences in 2012 and expires in 2017. The availability of this tax holiday did not have a significant impact on the Company's decision to increase its Asian presence, as the Company's decision was in response to market changes that took place in the semiconductor industry. This tax holiday had no dollar or per share effect in the three month periods ended January 29, 2012 and January 30, 2011.

NOTE 10 - EARNINGS PER SHARE

The calculation of basic and diluted earnings per share is presented below.

| | Three Months Ended | |
|---|---------------------|---------------------|
| | January 29, 2012 | January 30, 2011 |
| Net income attributable to Photronics, Inc. | \$4,268 | \$12,111 |
| Effect of dilutive securities: | | |
| Gains related to common stock warrants fair value adjustment | (94) | - |
| Interest expense on convertible notes, net of related tax effects | - | 1,022 |
| Earnings for diluted earnings per share | \$4,174 | \$13,133 |
| Weighted-average common shares computations: | | |
| Weighted-average common shares used for basic earnings per share | 59,817 | 53,817 |
| Effect of dilutive securities: | | |
| Share-based payment awards | 831 | 1,067 |
| Common stock warrants | 282 | 216 |
| Convertible notes | - | 11,311 |

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| | | |
|--|--------|--------|
| Potentially dilutive common shares | 1,113 | 12,594 |
| Weighted-average common shares used for diluted earnings per share | 60,930 | 66,411 |
| Basic earnings per share | \$0.07 | \$0.23 |
| Diluted earnings per share | \$0.07 | \$0.20 |

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The table below shows the outstanding weighted-average share-based payment awards and common stock warrants that were excluded from the calculation of diluted earnings per share because their exercise price exceeded the average market value of the common shares for the period or, under application of the treasury stock method, they were otherwise determined to be anti-dilutive. The table also shows convertible notes that, if converted, would have been anti-dilutive.

| | Three Months Ended | |
|--|---------------------|---------------------|
| | January 29, 2012 | January 30, 2011 |
| Convertible notes | 15,423 | - |
| Share-based payment awards | 2,550 | 2,816 |
| Common stock warrants | - | 299 |
| Total potentially dilutive shares excluded | 17,973 | 3,115 |

NOTE 11 – GEOGRAPHIC INFORMATION

The Company operates as a single operating segment as a manufacturer of photomasks, which are high precision quartz plates containing microscopic images of electronic circuits for use in the fabrication of ICs and FPDs. Geographic net sales are based primarily on where the Company's manufacturing facility is located. The Company's net sales by geographic area and for ICs and FPDs for the three month periods ended January 29, 2012 and January 30, 2011 and its long-lived assets by geographic area as of January 29, 2012, and October 30, 2011, are presented below.

| | Three Months Ended | |
|-------------------|---------------------|---------------------|
| | January 29, 2012 | January 30, 2011 |
| Net sales | | |
| Asia | \$ 70,236 | \$ 78,691 |
| Europe | 10,348 | 10,764 |
| North America | 31,570 | 31,368 |
| | \$ 112,154 | \$ 120,823 |
| IC | \$ 86,807 | \$ 88,801 |
| FPD | 25,347 | 32,022 |
| | \$ 112,154 | \$ 120,823 |
| | | As of |
| | January 29, 2012 | October 30, 2011 |
| Long-lived assets | | |
| Asia | \$ 198,071 | \$ 197,956 |
| Europe | 10,260 | 10,879 |
| North America | 151,483 | 159,845 |
| | \$ 359,814 | \$ 368,680 |

The Company is typically impacted during its first fiscal quarter by the North American and European holiday periods, as some customers reduce their effective workdays and orders during these periods. Additionally, the Company can be impacted during its first or second quarter by the Asian New Year holiday period, which may also

reduce customer orders.

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NOTE 12 - FAIR VALUE MEASUREMENTS

The accounting framework for determining fair value includes a hierarchy for ranking the quality and reliability of the information used to measure fair value, which enables the reader of the financial statements to assess the inputs used to develop those measurements. The fair value hierarchy consists of three tiers as follows: Level 1, defined as quoted market prices in active markets for identical securities; Level 2, defined as inputs other than Level 1 that are observable, either directly or indirectly; and Level 3, defined as unobservable inputs that are not corroborated by market data.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

The tables below present assets and liabilities as of October 30, 2011, that are measured at fair value on a recurring basis. The Company did not have any assets or liabilities measured at fair value on a recurring basis as of January 29, 2012.

| | October 30, 2011 | | | Total |
|-----------------------|--|---|--|----------|
| | Quoted Prices in Active Markets for Identical Instruments (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | |
| Common stock warrants | \$ - | \$ 1,147 | \$ - | \$ 1,147 |
| Total liabilities | \$ - | \$ 1,147 | \$ - | \$ 1,147 |

The fair value of the common stock warrants liability was determined using the Black-Scholes option pricing model. A significant observable input into the model included the market price of the Company's common stock at the measurement date. Gains or losses related to fair value adjustments to the common stock warrants liability are included in other income (expense), net.

Assets and Liabilities Measured at Fair Value on a Nonrecurring Basis

The Company did not have any nonfinancial assets or liabilities measured at fair value on a nonrecurring basis as of January 29, 2012 and October 30, 2011.

Fair Value of Other Financial Instruments

The fair values of the Company's cash and cash equivalents, accounts receivable, accounts payable, and certain other current assets and current liabilities approximate their carrying value due to their short-term maturities. The estimated fair value of the Company's 3.25% convertible senior notes was approximately \$ 118.1 million and \$109.3 million at January 29, 2012 and October 30, 2011, respectively, and the estimated fair value of the Company's 5.5% convertible senior notes was approximately \$35.5 million and \$32.8 million at January 29, 2012 and October 30, 2011, respectively.

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NOTE 13 - SUBSIDIARY SHARE REPURCHASE

During the three month period ended January 29, 2012, the board of directors of Photronics Semiconductor Mask Corporation (PSMC), a subsidiary of the Company based in Taiwan, authorized PSMC to repurchase for retirement up to 5% of its outstanding common stock on the open market. The repurchase program, which expires in March 2012 has, through January 29, 2012, resulted in 2.3 million shares (or 0.9 % of its outstanding shares) being repurchased at a total cost of \$0.9 million. PSMC's repurchase of these shares increased the Company's ownership of PSMC from 62.25% at October 30, 2011, to 62.80% at January 29, 2012. The tables below present the effect of the change in Photronics, Inc.'s ownership interest in PSMC on the Company's equity for the three month period ended January 29, 2012 and January 30, 2011.

| | Three Months Ended | |
|---|---------------------|---------------------|
| | January 29, 2012 | January 30, 2011 |
| Net income attributable to Photronics, Inc. | \$ 4,268 | \$ 12,111 |
| Increase in Photronics, Inc.'s additional paid-in capital for PSMC's repurchase of 2.3 million shares of its common stock | 151 | - |
| Change from net income attributable to Photronics, Inc. and transfer to noncontrolling interest | \$ 4,419 | \$ 12,111 |

NOTE 14 - COMMITMENTS AND CONTINGENCIES

As of January 29, 2012, the Company had commitments outstanding for capital expenditures of approximately \$1 million.

In connection with the Company's purchase of the U.S. nanoFab facility in the second quarter of fiscal 2012 (see Notes 3 and 4), the Company's lease agreement with Micron for the U.S. nanoFab facility was cancelled which reduced the Company's related outstanding operating lease commitments by a total of \$15 million for fiscal years 2013 and 2014.

The Company is subject to various claims that arise in the ordinary course of business. The Company believes such claims, individually or in the aggregate, will not have a material effect on its condensed consolidated financial statements.

NOTE 15 - RECENT ACCOUNTING PRONOUNCEMENTS

In June 2011 the FASB issued ASU No. 2011-05, "Presentation of Comprehensive Income", with the purpose of increasing the prominence of items reported in other comprehensive income. The amended guidance requires that all non-owner changes in stockholders' equity be presented either in a single continuous statement of comprehensive income or in two separate statements. The amendments also required that reclassification adjustments for items that are reclassified from other comprehensive income to net income in the statement(s) be presented on the face of the financial statements. However, in December 2011 the FASB issued ASU No. 2011-12 that deferred the effective date for amendments to the presentation of reclassifications of items out of other comprehensive income. ASU No. 2011-12 was issued to allow the FASB time to redeliberate whether it is necessary to require entities to present reclassification adjustments, by component, in both the statement where net income is presented and the statement where comprehensive income is presented for both interim and annual financial statements, as originally required under ASU No. 2011-05. During the FASB's redeliberation period, entities will continue to report reclassifications out of accumulated other comprehensive income using guidance in effect before ASU No. 2011-05 was issued. ASU No.

2011-05 is to be applied retrospectively and is effective for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2011. The adoption of this ASU will have no effect on the Company's reported financial condition, financial performance or cash flows.

In May 2011 the FASB issued ASU No. 2011-04, "Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs", which amended its guidance on fair value measurements with the purpose of achieving commonality of its fair value measurement and disclosure requirements with those of IFRSs. ASU No. 2011-04 clarifies the FASB's intentions regarding the application of existing fair value measurement and disclosure requirements, changes certain principles for measuring fair value and changes the disclosure requirements for fair value measurements. ASU No. 2011-04 is to be applied prospectively and is effective during interim and annual periods beginning after December 15, 2011. The Company is currently evaluating the effect, if any, ASU No. 2011-04 will have on its consolidated financial statements.

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Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

Management's discussion and analysis ("MD&A") of the Company's financial condition, results of operations and outlook should be read in conjunction with its condensed consolidated financial statements and related notes. Various segments of this MD&A contain forward-looking statements, all of which are presented based on current expectations and may be adversely affected by uncertainties and risk factors (presented throughout this filing and in the Company's Annual Report on Form 10-K for the fiscal 2011 year), that may cause actual results to materially differ from these expectations.

The Company sells substantially all of its photomasks to semiconductor designers and manufacturers, and manufacturers of FPDs. Photomask technology is also being applied to the fabrication of other higher performance electronic products such as photonics, micro-electronic mechanical systems and certain nanotechnology applications. Thus, the Company's selling cycle is tightly interwoven with the development and release of new semiconductor designs and flat panel applications, particularly as it relates to the semiconductor industry's migration to more advanced design methodologies and fabrication processes. The Company believes that the demand for photomasks primarily depends on design activity rather than sales volumes from products produced using photomask technologies. Consequently, an increase in semiconductor or FPD sales does not necessarily result in a corresponding increase in photomask sales. However, the reduced use of customized ICs, reductions in design complexity, other changes in the technology or methods of manufacturing or designing semiconductors, or a slowdown in the introduction of new semiconductor or FPD designs could reduce demand for photomasks even if demand for semiconductors and FPDs increases. Advances in semiconductor, FPD and photomask design and semiconductor production methods could reduce the demand for photomasks. Historically, the semiconductor industry has been volatile, with sharp periodic downturns and slowdowns. These downturns have been characterized by, among other things, diminished product demand, excess production capacity and accelerated erosion of selling prices.

The global semiconductor industry is driven by end markets which have been closely tied to consumer driven applications of high performance semiconductor devices including, but not limited to, mobile communications and computing solutions. The Company is typically required to fulfill its customer orders within a short period of time, sometimes within 24 hours. This results in the Company having a minimal level of backlog orders, typically one to two weeks for IC photomasks and two to three weeks for FPD photomasks. The Company cannot predict the timing of the industry's transition to volume production of next generation technology nodes or the timing of up and down cycles with precise accuracy, but believes that such transitions and cycles will continue into the future, beneficially and adversely affecting its business, financial condition and operating results in the near term. The Company believes its ability to remain successful in these environments is dependent upon achieving its goals of being a service and technology leader and efficient solutions supplier, which it believes should enable it to continually reinvest in its global infrastructure.

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Material Changes in Results of Operations

Three Months ended January 29, 2012 and January 30, 2011

The following table represents selected operating information expressed as a percentage of net sales.

| | Three Months Ended | |
|---|---------------------|---------------------|
| | January 29, 2012 | January 30, 2011 |
| Net sales | 100.0 % | 100.0 % |
| Cost of sales | (77.3) | (74.7) |
| Gross margin | 22.7 | 25.3 |
| Selling, general and administrative expenses | (10.1) | (8.9) |
| Research and development expenses | (4.0) | (3.1) |
| Consolidation, restructuring and related charges | (1.0) | - |
| Operating income | 7.6 | 13.3 |
| Other income (expense), net | (0.3) | 0.8 |
| Net income before income taxes | 7.3 | 14.1 |
| Income tax provision | (3.0) | (2.9) |
| Net income | 4.3 | 11.2 |
| Net income attributable to noncontrolling interests | (0.5) | (1.2) |
| Net income attributable to Photronics, Inc. | 3.8 % | 10.0 % |

Note: All of the following tabular comparisons, unless otherwise indicated, are for the three months ended January 29, 2012 (Q1-12) and January 30, 2011 (Q1-11) in millions of dollars.

Net Sales

| | Three Months Ended | | Percent Change |
|-----------------|--------------------|----------|-------------------|
| | Q1-12 | Q1-11 | |
| IC | \$ 86.8 | \$ 88.8 | (2.2)% |
| FPD | 25.4 | 32.0 | (20.8)% |
| Total net sales | \$ 112.2 | \$ 120.8 | (7.2)% |

Net sales for Q1-12 decreased 7.2% to \$112.2 million as compared to \$120.8 million for Q1-11. The decrease was primarily the result of lower unit demand and average selling prices (ASPs) for mainstream products for both IC and FPDs. Revenues attributable to high-end products increased by \$13.5 million to \$42.9 million in Q1-12 as compared to \$29.4 million in Q1-11, primarily as a result of increased ASPs and units for IC photomasks. High-end photomask applications, which typically have higher ASPs, include mask sets for 45 nanometer and below for IC products, and G8 and above and active matrix organic light-emitting diode (AMOLED) display screen technologies for FPD products. By geographic area, net sales in Q1-12 as compared to Q1-11 decreased by \$8.5 million or 10.7% in Asia, increased by \$0.2 million or 0.6% in North America, and decreased by \$0.4 million or 3.9% in Europe. As a percent of total net sales, net sales in Q1-12 in Asia were 63%, North America 28%, and Europe 9%, and net sales in Q1-11 in Asia were 65%, North America 26%, and Europe 9%.

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Gross Margin

| | Three Months Ended | | Percent Change |
|-------------------------|--------------------|---------|-------------------|
| | Q1-12 | Q1-11 | |
| Gross margin | \$ 25.5 | \$ 30.6 | (16.8)% |
| Percentage of net sales | 22.7% | 25.3% | |

Gross margin percentage decreased to 22.7% in Q1-12 as compared to 25.3% in Q1-11 as a result of decreased sales of mainstream IC and FPD products. The Company operates in a high fixed cost environment and, to the extent that the Company's revenues and utilization increase or decrease, gross margin will generally be positively or negatively impacted.

Selling, General and Administrative Expenses

| | Three Months Ended | | Percent Change |
|-------------------------|--------------------|---------|-------------------|
| | Q1-12 | Q1-11 | |
| S, G & A expenses | \$ 11.3 | \$ 10.7 | 5.7% |
| Percentage of net sales | 10.1% | 8.9% | |

Selling, general and administrative expenses increased \$0.6 million to \$11.3 million in Q1-12 as compared to \$10.7 million in Q1-11, primarily due to increased employee compensation and related benefit expenses.

Research and Development

| | Three Months Ended | | Percent Change |
|-------------------------|--------------------|--------|-------------------|
| | Q1-12 | Q1-11 | |
| R&D expenses | \$ 4.4 | \$ 3.8 | 17.8% |
| Percentage of net sales | 4.0% | 3.1% | |

Research and development expenses consist primarily of global development efforts related to high-end process technologies for advanced sub-wavelength reticle solutions for IC technologies. Research and development expenses increased \$0.6 million in Q1-12 as compared to Q1-11 primarily as a result of increased expenditures in the U.S.

Consolidation, Restructuring and Related Charges

| | Three Months Ended | |
|--|--------------------|-------|
| | Q1-12 | Q1-11 |
| Employee terminations and other | \$ 886 | \$ - |
| Asset write-downs | 232 | - |
| Total consolidation, restructuring and related charges | \$ 1,118 | \$ - |

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In the first quarter of fiscal 2012, the Company ceased the manufacture of photomasks at its Singapore facility, and in connection therewith recorded a charge of \$1.1 million during the three month period ended January 29, 2012. The Company expects that this restructuring will be completed in fiscal 2012, and expects its total cost to range between \$1.5 million and \$1.9 million, with that cost primarily being comprised of employee termination costs and asset write-downs.

Other Income (Expense), net

| | Three Months Ended | |
|----------------------------------|--------------------|-----------|
| | Q1-12 | Q1-11 |
| Interest expense | \$ (1.8) | \$ (1.7) |
| Investment and other income, net | 1.4 | 2.7 |
| Other income (expense), net | \$ (0.4) | \$ 1.0 |

Other income (expense) net decreased in Q1-12 as compared to Q1-11 primarily as a result of less favorable foreign currency transaction results.

Provision for Income Taxes

| | Three Months Ended | |
|---------------------------|--------------------|--------|
| | Q1-12 | Q1-11 |
| Income tax provision | \$ 3.3 | \$ 3.5 |
| Effective income tax rate | 40.7 % | 20.4 % |

The effective income tax rate in the first quarter of fiscal 2012 increased from the first quarter of fiscal 2011 primarily because income tax provisions recorded in jurisdictions in which the Company generated income before income taxes were, due to valuation allowances, not significantly offset by income tax benefits recorded in jurisdictions in which the Company incurred losses before income taxes.

PKLT, the Company's FPD manufacturing facility in Taiwan, is accorded a tax holiday which commences in 2012 and expires in 2017. The availability of this tax holiday did not have a significant impact on the Company's decision to increase its Asian presence, as the Company's decision was in response to market changes that took place in the semiconductor industry. This tax holiday had no dollar or per share effect in the three month periods ended January 29, 2012 and January 30, 2011.

Net Income Attributable to Noncontrolling Interests

Net income attributable to noncontrolling interests decreased \$0.9 million to \$0.6 million in Q1-12 as compared to \$1.5 million in Q1-11, primarily due to decreased net income at the Company's non-wholly owned subsidiary in Taiwan. As a result of share repurchase programs in 2011 and 2012, the Company's ownership percentage in this subsidiary increased by approximately 5%. The Company's ownership in this subsidiary in Taiwan was approximately 62.80% at January 29, 2012 and 62.25% October 30, 2011, and its ownership in its subsidiary in Korea was approximately 99.7% at January 29, 2012 and October 30, 2011.

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Liquidity and Capital Resources

The Company's working capital was \$220.5 million at January 29, 2012, and \$209.3 million at October 30, 2011. The increase in working capital was the result of cash generated by operating activities. The increase in cash and cash equivalents to \$201.8 million at January 29, 2012, as compared to \$189.9 million at October 30, 2011, was also the result of cash generated by operating activities. Net cash provided by operating activities was \$34.0 million for the three months ended January 29, 2012, as compared to \$41.7 million for the three month period ended January 30, 2011, the decrease primarily being due to lower net income. Net cash used in investing activities for the three months ended January 29, 2012, was \$20.1 million, which was comprised primarily of capital expenditure payments. Net cash used in financing activities of \$1.7 million for the three months ended January 29, 2012, was primarily comprised of repayments of long-term borrowings and payments to repurchase the common stock of a subsidiary.

The Company's revolving credit facility ("the credit facility") provides for a maximum borrowing capacity of \$30 million. The credit facility bears interest (2.5% at January 29, 2012) at LIBOR plus a spread based upon the Company's total leverage ratio, as defined in the agreement. As of January 29, 2012, the Company had no outstanding borrowings under the credit facility and \$30 million was available for borrowing. The credit facility, which matures in April 2015, is secured by substantially all of the Company's assets located in the United States as well as common stock the Company owns in certain of its foreign subsidiaries. The credit facility is subject to the following financial covenants: minimum fixed charge ratio, total leverage ratio and minimum unrestricted cash balance.

In the second quarter of fiscal 2012 the Company paid \$35 million to Micron in connection with the purchase of the U.S. nanoFab facility and in connection therewith amended the credit facility, which included the addition of a \$25 million term loan maturing in March 2017, with quarterly principal payments of \$0.6 million (quarterly payments are based on a ten year repayment period commencing in June 2012). The amendment also included a twenty-five basis point reduction in the interest rate charged on any borrowings under the credit facility. As a result of the purchase of the U.S. nanoFab facility, the Company's lease agreement with Micron for the U.S. nanoFab facility was cancelled, which reduced the Company's related outstanding operating lease commitments by a total of \$15 million for fiscal years 2013 and 2014.

At January 29, 2012, the Company had capital commitments outstanding of approximately \$1 million. The Company believes that its currently available resources, together with its capacity for growth, and its access to equity and other financing sources, will be sufficient to satisfy its currently planned capital expenditures, as well as its anticipated working capital requirements for the next twelve months. However, the Company cannot assure that additional sources of financing would be available to the Company on commercially favorable terms should the Company's capital requirements exceed cash available from operations, existing cash, and cash available under its credit facility.

The Company's liquidity is highly dependent on its sales volume, cash conversion cycle, and the timing of its capital expenditures (which can vary significantly from period to period), as it operates in a high fixed cost environment. Although the Company continues to evaluate further cost reduction initiatives, depending on conditions in the semiconductor and FPD markets, the Company's cash flows from operations and current holdings of cash may not be adequate to meet its current and long-term needs for capital expenditures, operations and debt repayments. Historically, in certain years the Company has used external financing to fund these needs. Due to conditions in the credit markets, some financing instruments used by the Company in the past may not be currently available to it. The Company cannot assure that additional sources of financing would be available to it on commercially favorable terms should its cash requirements exceed cash available from operations, existing cash, and cash available under its credit facility.

Off-Balance Sheet Arrangements

Under the MP Mask joint venture operating agreement, in order to maintain its 49.99% ownership interest, the Company may be required to make additional capital contributions to the joint venture up to the maximum amount specified in the operating agreement. Cumulatively through January 29, 2012, the Company has contributed \$25.1 million to the joint venture, and has received distributions from the joint venture totaling \$10.0 million. In March 2012 the Company made an additional capital contribution to MP Mask of \$5.5 million.

The Company leases certain office facilities and equipment under operating leases that may require it to pay taxes, insurance and maintenance expenses related to the properties. Certain of these leases contain renewal or purchase options exercisable at the end of the lease terms.

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Business Outlook

A majority of the Company's revenue growth is expected to continue to come from the Asian region, as customers increase their use of manufacturing foundries located outside of North America and Europe. Additional revenue growth is also anticipated in North America, as the Company benefits from advanced technology it may utilize under its technology license with Micron. The Company's Korean and Taiwanese operations are non-wholly owned subsidiaries and, therefore, a portion of earnings generated at each of these locations is allocated to noncontrolling interests.

The Company continues to assess its global manufacturing strategy and monitor its market capitalization, sales volume and related cash flows from operations. This ongoing assessment could result in future facility closures, asset redeployments, additional impairments of intangible or long-lived assets, workforce reductions, or the addition of increased manufacturing facilities, all of which would be based on market conditions and customer requirements.

Effect of Recent Accounting Pronouncements

See Note 15 of the condensed consolidated financial statements for a summary of recent accounting pronouncements that may affect the Company's financial reporting.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company records derivatives on the condensed consolidated balance sheets as assets or liabilities, measured at fair value. The Company does not engage in derivative instruments for speculative purposes. Gains or losses resulting from changes in the values of those derivatives are reported in the condensed consolidated statements of operations, or as accumulated other comprehensive income or loss, a separate component of equity, depending on the use of the derivatives and whether they qualify for hedge accounting. In order to qualify for hedge accounting, among other criteria, the derivative must be a hedge of an interest rate, price, foreign currency exchange rate, or credit risk, that is expected to be highly effective at the inception of the hedge and be highly effective in achieving offsetting changes in the fair value or cash flows of the hedged item during the term of the hedge, and formally documented at the inception of the hedge. The types of risks hedged are those related to the variability of future cash flows caused by movements in foreign currency exchange and interest rates. The Company documents its risk management strategy and hedge effectiveness at the inception of, and during the term of each hedge.

Foreign Currency Exchange Rate Risk

The Company conducts business in several major international currencies through its worldwide operations and its financial performance may be affected by fluctuations in the exchange rates of these currencies. Changes in exchange rates can positively or negatively affect the Company's sales, operating margins, assets, liabilities, and equity. The functional currencies of the Company's Asian subsidiaries are the Korean won, the New Taiwan dollar, and the Singapore dollar. The functional currencies of the Company's European subsidiaries are the British pound and the euro.

The Company attempts to minimize its risk of foreign currency transaction losses by producing its products in the same country in which the products are sold (thereby generating revenues and incurring expenses in the same currency), and by managing its working capital. In some instances, the Company may sell or purchase products in a currency other than the functional currency of the country where it was produced. There can be no assurance that this approach will continue to be successful, especially in the event of a significant adverse movement in the value of any foreign currencies against the U.S. dollar. In certain prior years the Company experienced significant foreign exchange losses on these transactions.

The Company's primary net foreign currency exposures as of January 29, 2012, included the Korean won, the Japanese yen, the New Taiwan dollar, the Singapore dollar, the British pound, and the euro. As of January 29, 2012, a 10% adverse movement in the value of these currencies against the U.S. dollar would have resulted in a net unrealized pre-tax loss of \$2.5 million. The Company does not believe that a 10% change in the exchange rates of other non-U.S. dollar currencies would have a material effect on its consolidated financial position, results of operations, or cash flows.

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Interest Rate Risk

At January 29, 2012, the Company did not have any outstanding variable rate borrowings. A change in interest rates would not have had a material effect on the Company's consolidated financial position, results of operations, or cash flows in the three month period ended January 29, 2012.

Item 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

The Company has established and currently maintains disclosure controls and procedures, as such term is defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), designed to ensure that information required to be disclosed in its reports filed under the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to management, including the Company's chief executive officer and chief financial officer, as appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

The Company's management, under the supervision and with the participation of the Company's chief executive officer and chief financial officer, evaluated the effectiveness of the design and operation of the Company's disclosure controls and procedures as of the end of the period covered by this report. Based upon that evaluation the Company's chief executive officer and chief financial officer concluded that the Company's disclosure controls and procedures were effective at a reasonable assurance level as of the end of the period covered by this report.

Changes in Internal Control over Financial Reporting

There was no change in the Company's internal control over financial reporting during the Company's first quarter of fiscal 2012 that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

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PART II. OTHER INFORMATION

Item 1A. RISK FACTORS

There have been no material changes to risks relating to the Company's business as disclosed in Part 1, Item 1A of the Company's Form 10-K for the year ended October 30, 2011.

Item 6. EXHIBITS

(a) Exhibits

| Exhibit Number | Description |
|----------------|---|
| <u>31.1</u> | Certification of Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| <u>31.2</u> | Certification of Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| <u>32.1</u> | Certification of Chief Executive Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| <u>32.2</u> | Certification of Chief Financial Officer 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 Extension Calculation Linkbase Document |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document |
| 101.LAB | XBRL Taxonomy Extension Label Linkbase Document |
| 101.PRE | XBRL Taxonomy Extension Presentation Linkbase Document |

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.

Photronics, Inc.
(Registrant)

By: /s/ SEAN T. SMITH

Sean T. Smith
Senior Vice President
Chief Financial Officer
(Duly Authorized Officer and
Principal Financial Officer)

Date: March 7, 2012

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