Proto Labs Inc
Form 10-Q
August 06, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 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 June 30, 2015

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: 001-35435

Proto Labs, Inc.

(Exact name of registrant as specified in its charter)

Minnesota	**41-1939628**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
5540 Pioneer Creek Drive	
Maple Plain, Minnesota	**55359**
(Address of principal executive offices)	(Zip Code)

(763) 479-3680

(Registrant's telephone number, including area code)

Not Applicable

(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 Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T 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.

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 26,136,434 shares of Common Stock, par value $0.001 per share, were outstanding at July 30, 2015.

Proto Labs, Inc.

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Proto Labs, Inc.
Consolidated Balance Sheets
(In thousands, except share and per share amounts)

	June 30, 2015 (Unaudited)	**December 31, 2014**
Assets		
Current assets		
Cash and cash equivalents	$ 56,324	$ 43,329
Short-term marketable securities	31,190	30,706
Accounts receivable, net of allowance for doubtful accounts of $150 and $198 as of June 30, 2015 and December 31, 2014, respectively	29,493	24,226
Inventory	6,828	6,194
Prepaid expenses and other current assets	3,935	3,406
Income taxes receivable	2,931	-
Deferred tax assets	464	483
Total current assets	131,165	108,344
Property and equipment, net	100,921	91,626
Goodwill	28,916	28,916
Other intangible assets, net	3,710	4,083
Long-term marketable securities	54,482	54,318
Other long-term assets	197	227
Total assets	$ 319,391	$ 287,514
Liabilities and shareholders' equity		
Current liabilities		
Accounts payable	$ 11,334	$ 7,882
Accrued compensation	8,264	6,067
Accrued liabilities and other	1,779	2,718
Income taxes payable	-	1,953
Current portion of long-term debt obligations	71	139
Total current liabilities	21,448	18,759
Long-term deferred tax liabilities	2,423	1,846
Long-term debt obligations	-	10
Other long-term liabilities	1,533	1,360

Total liabilities	25,404	21,975
Shareholders' equity		
Preferred stock, $0.001 par value, authorized 10,000,000 shares; issued and outstanding 0 shares as of each of June 30, 2015 and December 31, 2014	-	-
Common stock, $0.001 par value, authorized 150,000,000 shares; issued and outstanding 25,953,735 and 25,838,110 shares as of June 30, 2015 and December 31, 2014, respectively	26	26
Additional paid-in capital	187,070	180,960
Retained earnings	109,621	87,482
Accumulated other comprehensive loss	(2,730)	(2,929)
Total shareholders' equity	293,987	265,539
Total liabilities and shareholders' equity	$ 319,391	$ 287,514

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

Proto Labs, Inc.
Consolidated Statements of Comprehensive Income
(In thousands, except share and per share amounts)
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2015	**2014**	**2015**	**2014**
Statements of Operations:				
Revenue	$63,969	$52,866	$122,505	$98,940
Cost of revenue	26,419	20,183	49,701	37,233
Gross profit	37,550	32,683	72,804	61,707
Operating expenses				
Marketing and sales	9,502	7,261	18,356	13,678
Research and development	4,397	3,914	8,711	7,370
General and administrative	6,304	5,534	12,549	10,237
Total operating expenses	20,203	16,709	39,616	31,285
Income from operations	17,347	15,974	33,188	30,422
Other income (expense), net	(36)	(66)	(493)	37
Income before income taxes	17,311	15,908	32,695	30,459
Provision for income taxes	5,625	4,952	10,556	9,401
Net income	$11,686	$10,956	$22,139	$21,058
Net income per share:				
Basic	$0.45	$0.43	$0.86	$0.82
Diluted	$0.44	$0.42	$0.84	$0.81
Shares used to compute net income per share:				
Basic	25,921,111	25,620,005	25,885,888	25,597,055
Diluted	26,277,503	26,146,848	26,245,135	26,132,265
Comprehensive Income (net of tax)				
Comprehensive income	$12,960	$11,488	$22,338	$21,762

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

Proto Labs, Inc.
Consolidated Statements of Cash Flows
(In thousands)
(Unaudited)

	Six Months Ended June 30, 2015	2014
Operating activities		
Net income	$22,139	$21,058
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	6,940	4,683
Stock-based compensation expense	2,909	2,248
Deferred taxes	620	107
Excess tax benefit from stock-based compensation	(989)	(1,623)
Amortization of held-to-maturity securities	632	854
Changes in operating assets and liabilities:		
Accounts receivable	(5,219)	(5,742)
Inventories	(663)	(306)
Prepaid expenses and other	(469)	(372)
Income taxes	(3,687)	2,431
Accounts payable	3,377	5,143
Accrued liabilities and other	2,243	(2,464)
Net cash provided by operating activities	27,833	26,017
Investing activities		
Purchases of property and equipment	(15,717)	(31,625)
Acquisitions, net of cash acquired	-	(33,864)
Purchases of marketable securities	(25,389)	(38,463)
Proceeds from sales and maturities of marketable securities	24,109	55,441
Net cash used in investing activities	(16,997)	(48,511)
Financing activities		
Payments on debt	(77)	(954)
Acquisition-related contingent consideration	(1,000)	(400)
Proceeds from exercises of stock options and other	2,207	1,806
Excess tax benefit from stock-based compensation	989	1,623
Net cash provided by financing activities	2,119	2,075
Effect of exchange rate changes on cash and cash equivalents	40	234
Net increase (decrease) in cash and cash equivalents	12,995	(20,185)
Cash and cash equivalents, beginning of period	43,329	43,039
Cash and cash equivalents, end of period	$56,324	$22,854

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

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Note 1 – Basis of Presentation

The unaudited interim Consolidated Financial Statements of Proto Labs, Inc. (Proto Labs, the Company, we, us or our) have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. These statements are unaudited but, in the opinion of management, reflect all adjustments necessary for a fair presentation of the Company's statement of financial position, results of operations and cash flows for the periods presented. Except as otherwise disclosed herein, these adjustments consist of normal, recurring items. Operating results for interim periods are not necessarily indicative of results that may be expected for the fiscal year as a whole.

On April 23, 2014, the Company completed the acquisition of FineLine Prototyping, Inc. (FineLine). The operations of FineLine have been integrated into the operations of the Company and operating results beginning April 23, 2014 are included in the consolidated results under the Fineline product line.

The preparation of the financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses, and the related disclosures at the date of the financial statements and during the reporting period. Actual results could materially differ from these estimates. For further information, refer to the audited consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2014 as filed with the Securities and Exchange Commission (SEC) on February 27, 2015.

The accompanying Consolidated Balance Sheet as of December 31, 2014 was derived from the audited Consolidated Financial Statements but does not include all disclosures required by U.S. GAAP for a full set of financial statements. This Form 10-Q should be read in conjunction with the Company's Consolidated Financial Statements and Notes included in the Annual Report on Form 10-K filed on February 27, 2015 as referenced above.

Note 2 – Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) No. 2014-09, Revenue from Contracts with Customers. This ASU is a comprehensive new revenue recognition model that requires a company to recognize revenue from the transfer of goods or services to customers in an amount that reflects the consideration that the entity expects to receive in exchange for those goods or services. The Company is required to adopt the new pronouncement using one of two retrospective application methods.

On July 9, 2015, the FASB voted to approve a one-year deferral of the effective date of ASU 2014-09 by one year to December 15, 2017 for annual reporting periods beginning after that date. The Company is evaluating the application method and the impact of this new standard on our financial statements, but does not expect the impact to be material.

Note 3 – Net Income per Common Share

Basic net income per share is computed based on the weighted-average number of common shares outstanding. Diluted net income per share is computed based on the weighted-average number of common shares outstanding, increased by the number of additional shares that would have been outstanding had potentially dilutive common shares been issued and reduced by the number of shares the Company could have repurchased from the proceeds from issuance of the potentially dilutive shares. Potentially dilutive shares of common stock include stock options, restricted stock units and restricted stock awards granted under stock-based compensation plans and shares committed to be purchased under the employee stock purchase plan.

The table below sets forth the computation of basic and diluted net income per share:

(in thousands, except share and per share amounts)	Three Months Ended June 30, 2015	2014	Six Months Ended June 30, 2015	2014
Net income	$11,686	$10,956	$22,139	$21,058
Basic - weighted-average shares outstanding:	25,921,111	25,620,005	25,885,888	25,597,055
Effect of dilutive securities:				
Employee stock options and other	356,392	526,843	359,247	535,210
Diluted - weighted-average shares outstanding:	26,277,503	26,146,848	26,245,135	26,132,265
Net income per share:				
Basic	$0.45	$0.43	$0.86	$0.82
Diluted	$0.44	$0.42	$0.84	$0.81

Note 4 – Goodwill and Other Intangible Assets

The changes in the carrying amount of Goodwill during the six months ended June 30, 2015 were as follows:

(in thousands)	Six Months Ended June 30, 2015
Balance as of the beginning of the period	$28,916
Goodwill acquired during the period	-
Balance as of the end of the period	$28,916

Intangible assets other than Goodwill at June 30, 2015 and December 31, 2014 were as follows:

	June 30, 2015			December 31, 2014			Useful	Weighted Average
		Accumulated			Accumulated		Life	Useful Life
(in thousands)	Gross	Amortization	Net	Gross	Amortization	Net		

								(in years)	Remaining (in years)
Intangible Assets with finite lives:									
Marketing assets	$930	$	(109)	$821	$930	$	(62)	$868	10.0	8.8
Non-compete agreement	190		(111)	79	190		(63)	127	2.0	0.8
Trade secrets	250		(58)	192	250		(33)	217	5.0	3.8
Internally developed software	680		(264)	416	680		(151)	529	3.0	1.8
Customer relationships	2,530		(328)	2,202	2,530		(188)	2,342	9.0	7.8
Total intangible assets	$4,580	$	(870)	$3,710	$4,580	$	(497)	$4,083		

Amortization expense for intangible assets for the three and six months ended June 30, 2015 was $0.2 million and $0.4 million, respectively. Amortization expense for intangible assets, which were acquired in the purchase of FineLine in April 2014, was $0.1 million for each of the three and six months ended June 30, 2014.

Estimated aggregated amortization expense based on the current carrying value of the amortizable intangible assets is as follows:

(in thousands)	**Estimated Amortization Expense**
Remaining 2015	$ 373
2016	682
2017	500
2018	424
2019	391
Thereafter	1,340
Total estimated amortization expense	$ 3,710

Note 5 – Fair Value Measurements

ASC 820, *Fair Value Measuremen*t (ASC 820), defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. ASC 820 also establishes a fair value hierarchy which requires classification based on observable and unobservable inputs when measuring fair value. There are three levels of inputs that may be used to measure fair value:

Level 1—Quoted prices in active markets for identical assets or liabilities.

Level 2—Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3—Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The Company's cash consists of bank deposits. The Company's cash equivalents measured at fair value consist of money market mutual funds. The Company determines the fair value of these investments using Level 1 inputs.

A summary of financial assets as of June 30, 2015 and December 31, 2014 measured at fair value on a recurring basis follows:

	June 30, 2015			**December 31, 2014**		
(in thousands)	**Level 1**	**Level 2**	**Level 3**	**Level 1**	**Level 2**	**Level 3**
Financial Assets:						
Cash and cash equivalents						
Money market mutual fund	$15,761	$ -	$ -	$6,129	$ -	$ -
Total	$15,761	$ -	$ -	$6,129	$ -	$ -

Note 6 – Marketable Securities

The Company invests in short-term and long-term agency, municipal, corporate, commercial paper and other debt securities. The securities are categorized as held-to-maturity and are recorded at amortized cost. Categorization as held-to-maturity is based on the Company's ability and intent to hold these securities to maturity. Information regarding the Company's short-term and long-term marketable securities as of June 30, 2015 and December 31, 2014 is as follows:

(in thousands)	June 30, 2015 Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. municipal securities	$32,661	$ 20	$ (49)	$32,632
Corporate debt securities	25,932	5	(31)	25,906
U.S. government agency securities	19,857	9	(23)	19,843
Certificates of deposit/time deposits	5,656	12	-	5,668
Commercial paper	1,566	-	(1)	1,565
Total marketable securities	$85,672	$ 46	$ (104)	$85,614

(in thousands)	December 31, 2014 Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. municipal securities	$30,004	$ 32	$ (18)	$30,018
Corporate debt securities	29,316	7	(79)	29,244
U.S. government agency securities	20,048	-	(71)	19,977
Certificates of deposit/time deposits	5,656	5	(15)	5,646
Total marketable securities	$85,024	$ 44	$ (183)	$84,885

Fair values for the corporate debt securities are primarily determined based on quoted market prices (Level 1). Fair values for the U.S. municipal securities, U.S. government agency securities, certificates of deposit and commercial paper are primarily determined using dealer quotes or quoted market prices for similar securities (Level 2).

The Company tests for other-than-temporary losses on a quarterly basis and has considered the unrealized losses indicated above, which are the result of changes in interest rates, to be temporary in nature. In reaching this conclusion, the Company considered the credit quality of the issuers of the debt securities as well as the Company's intent to hold the investments to maturity and recover the full principal.

Classification of marketable securities as current or non-current is based upon the security’s maturity date as of the date of these financial statements.

The June 30, 2015 balance of held-to-maturity debt securities by contractual maturity is shown in the following table at amortized cost. Actual maturities may differ from contractual maturities because the issuers of the securities may have the right to prepay obligations without prepayment penalties.

(in thousands)	**June 30, 2015**
Due in one year or less	$31,190
Due after one year through five years	54,482
Total marketable securities	$85,672

Note 7 – Inventory

Inventory consists primarily of raw materials, which are recorded at the lower of cost or market using the average-cost method, which approximates first-in, first-out (FIFO) cost. The Company periodically reviews its inventory for slow-moving, damaged and discontinued items and provides allowances to reduce such items identified to their recoverable amounts.

The Company’s inventory consists of the following:

(in thousands)	**June 30, 2015**	**December 31, 2014**
Raw materials	$6,108	$ 5,728
Work in process	922	653
Total inventory	7,030	6,381
Allowance for obsolescence	(202)	(187)
Inventory, net of allowance	$6,828	$