CTI INDUSTRIES CORP
Form 10-Q
May 16, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 2011

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
000-23115

CTI INDUSTRIES CORPORATION
(Exact name of Registrant as specified in its charter)

Illinois (State or other jurisdiction of incorporation or organization)	36-2848943 (I.R.S. Employer Identification Number)
22160 N. Pepper Road Lake Barrington, Illinois (Address of principal executive offices)	60010 (Zip Code)

(847) 382-1000
(Registrant's telephone number, including area code)

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 þ No o

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 þ No o

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer, or a smaller reporting company. See definition of “large accelerated filer”, “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer o Accelerated filer o Non-accelerated filer o Smaller Reporting Company þ

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

The number of shares outstanding of the Registrant’s common stock as of May 1, 2011 was 3,137,848.

INDEX

PART I – FINANCIAL INFORMATION

PART II – OTHER INFORMATION

PART 1 - FINANCIAL INFORMATION

Item 1. Financial Statements

CTI Industries Corporation and Subsidiaries
Condensed Consolidated Balance Sheets

	March 31, 2011 (unaudited)	December 31, 2010
ASSETS		
Current assets:		
Cash and cash equivalents (VIE $8,000 and $38,000, respectively)	$ 400,914	$ 761,874
Accounts receivable, (less allowance for doubtful accounts of $66,000 and $59,000, respectively)	10,052,699	8,533,626
Inventories, net	11,033,046	10,368,037
Net deferred income tax asset	701,955	750,485
Prepaid expenses and other current assets	1,643,538	1,012,067
Total current assets	23,832,152	21,426,089
Property, plant and equipment:		
Machinery and equipment	23,739,425	22,900,460
Building	3,280,245	3,260,201
Office furniture and equipment	2,795,250	2,718,425
Intellectual property	345,092	345,092
Land	250,000	250,000
Leasehold improvements	452,551	443,630
Fixtures and equipment at customer locations	2,629,902	2,629,902
Projects under construction (VIE $636,000 and $587,000, respectively)	1,023,167	1,601,682
	34,515,632	34,149,392
Less : accumulated depreciation and amortization	(24,995,066)	(24,489,624)
Total property, plant and equipment, net	9,520,566	9,659,768
Other assets:		
Deferred financing costs, net	56,816	63,634
Goodwill	1,033,077	1,033,077
Net deferred income tax asset	369,697	360,830
Other assets (due from related party $32,000 and $213,000, respectively)	144,242	317,990
Total other assets	1,603,832	1,775,531
TOTAL ASSETS	$ 34,956,550	$ 32,861,388
LIABILITIES AND EQUITY		
Current liabilities:		
Checks written in excess of bank balance	$ 610,433	$ 692,141
Trade payables (VIE $25,000 and $58,000, respectively)	5,076,371	4,307,358
Line of credit (VIE $760,000 and $700,000, respectively)	8,518,498	8,225,900
Notes payable - current portion	93,334	276,667

Notes payable - officers, current portion, net of debt discount of $0 and $5,000	1,581,237	1,410,807
Capital lease - current portion	5,117	5,117
Notes Payable Affiliates - current portion	7,210	6,754
Accrued liabilities	3,112,708	3,027,298
Total current liabilities	19,004,908	17,952,042
Long-term liabilities:		
Notes Payable - Affiliates	162,624	155,648
Notes payable, net of current portion	3,252,756	2,611,127
Capital Lease	1,279	2,559
Notes payable - officers, subordinated, net of debt discount of $0 and $0	440	360,351
Total long-term liabilities	3,417,099	3,129,685
Equity:		
CTI Industries Corporation stockholders' equity:		
Preferred Stock – no par value 2,000,000 shares authorized 0 shares issued and outstanding	-	-
Common stock - no par value, 5,000,000 shares authorized, 3,209,975 and 3,209,475 shares issued and 3,137,848 and 3,137,348 outstanding, respectively	13,397,275	13,394,940
Paid-in-capital	852,141	817,138
Dividends	-	(314,441)
Accumulated deficit	(396,543)	(379,210)
Accumulated other comprehensive loss	(1,140,167)	(1,592,798)
Less: Treasury stock, 72,127 shares and 72,127 shares	(141,289)	(141,289)
Total CTI Industries Corporation stockholders' equity	12,571,417	11,784,340
Noncontrolling interest	(36,874)	(4,679)
Total Equity	12,534,543	11,779,661
TOTAL LIABILITIES AND EQUITY	$ 34,956,550	$ 32,861,388

See accompanying notes to condensed consolidated unaudited financial statements

CTI Industries Corporation and Subsidiaries
Condensed Consolidated Statements of Operations (Unaudited)

	For the Three Months Ended March 31, 2011	2010
Net Sales	$ 12,697,655	$ 12,410,766
Cost of Sales	10,226,883	9,366,194
Gross profit	2,470,772	3,044,572
Operating expenses:		
General and administrative	1,329,954	1,260,679
Selling	214,254	340,425
Advertising and marketing	328,133	483,412
Total operating expenses	1,872,341	2,084,516
Income from operations	598,431	960,056
Other (expense) income:		
Interest expense	(141,235)	(248,403)
Interest income	2,029	4,330
Foreign currency gain (loss)	11,117	(13,223)
Total other expense, net	(128,089)	(257,296)
Net Income before taxes	470,342	702,760
Income tax expense	205,429	116,359
Net Income	264,913	586,401
Less: Net loss attributable to noncontrolling interest	(32,195)	(12,443)
Net income attributable to CTI Industries Corporation	$ 297,108	$ 598,844
Other Comprehensive Income		
Adjustment to accumulated balance on swap termination (2009); unrealized gain on derivative instruments (2010)	$ -	$ 34,197
Foreign currency adjustment	452,631	219,792
Comprehensive income	$ 749,739	$ 852,833
Basic income per common share	$ 0.09	$ 0.22
Diluted income per common share	$ 0.09	$ 0.21
Dividends per share	$ -	$ -

Weighted average number of shares and equivalent shares of common stock outstanding:		
Basic	3,137,837	2,769,002
Diluted	3,198,742	2,793,863

See accompanying notes to condensed consolidated unaudited financial statements

2

CTI Industries Corporation and Subsidiaries
Condensed Consolidated Statements of Cash Flows (Unaudited)

	For the Three Months Ended March 31, 2011	2010
Cash flows from operating activities:		
Net income	$ 264,913	$ 586,401
Adjustment to reconcile net income to cash (used in) provided by operating activities:		
Depreciation and amortization	454,306	495,579
Amortization of debt discount	5,042	22,167
Stock based compensation	35,003	47,013
Provision for losses on accounts receivable	7,275	25,402
Provision for losses on inventories	51,572	9,984
Deferred income taxes	69,952	86,359
Change in assets and liabilities:		
Accounts receivable	(1,416,729)	(1,302,167)
Inventories	(621,125)	(409,659)
Prepaid expenses and other assets	(465,295)	39,120
Trade payables	721,348	364,426
Accrued liabilities	306,682	279,076
Net cash (used in) provided by operating activities	(587,056)	243,701
Cash used in investing activities - purchases of property, plant and equipment	(253,262)	(197,167)
Net cash used in investing activities	(253,262)	(197,167)
Cash flows from financing activities:		
Change in checks written in excess of bank balance	(83,765)	93,435
Net change in revolving line of credit	290,175	(68,172)
Proceeds from issuance of long-term debt	598,296	-
Repayment of long-term debt (related parties $227,000 and $47,000)	(345,536)	(411,738)
Proceeds from exercise of stock options and warrants	2,335	48,737
Cash received from investment in subsidiary	-	42,299
Cash paid for deferred financing fees	-	(6,813)
Net cash provided by (used in) financing activities	461,505	(302,252)
Effect of exchange rate changes on cash	17,883	19,470
Net decrease in cash and cash equivalents	(360,960)	(236,248)
Cash and cash equivalents at beginning of period	761,874	914,765
Cash and cash equivalents at end of period	$ 400,914	$ 678,517

Supplemental disclosure of cash flow information:		
Cash payments for interest	$ 127,448	$ 211,756
Cash payments for taxes	$ 25,000	$ -
Supplemental Disclosure of non-cash investing and financing activity		
Property, Plant & Equipment acquisitions funded by liabilities	$ 33,550	$ 40,448

See accompanying notes to condensed consolidated unaudited financial statements

CTI Industries Corporation and Subsidiaries
Condensed Consolidated Earnings per Share (unaudited)

	Three Months Ended March 31, 2011	2010
Basic		
Average shares outstanding:		
Weighted average number of common shares outstanding	3,137,837	2,769,002
Net income:		
Net income attributable to CTI Industries Corporation	$ 297,108	$ 598,844
Per share amount	$ 0.09	$ 0.22
Diluted		
Average shares outstanding:		
Weighted average number of common shares outstanding	3,137,837	2,769,002
Effect of dilutive shares	60,905	24,861
Weighted average number of shares and equivalent shares of common stock outstanding	3,198,742	2,793,863
Net income:		
Net income attributable to CTI Industries Corporation	$ 297,108	$ 598,844
Per share amount	$ 0.09	$ 0.21

See accompanying notes to condensed consolidated unaudited financial statements

CTI Industries Corporation and Subsidiaries
Notes to Unaudited Condensed Consolidated Financial Statements

Note 1 - Basis of Presentation

The accompanying condensed consolidated financial statements are unaudited but in the opinion of management contain all the adjustments (consisting of those of a normal recurring nature) considered necessary to present fairly the consolidated financial position and the consolidated results of operations and consolidated cash flows for the periods presented in conformity with generally accepted accounting principles for interim consolidated financial information and the instructions to Form 10-Q and Article 8 of Regulation S-X. Accordingly, they do not include all the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. Operating results for the three months ended March 31, 2011 are not necessarily indicative of the results that may be expected for the fiscal year ending December 31, 2011. It is suggested that these condensed financial statements be read in conjunction with the consolidated financial statements and notes thereto included in the Company's annual report on Form 10-K for the fiscal year ended December 31, 2010.

Principles of consolidation and nature of operations:

The condensed consolidated financial statements include the accounts of CTI-US and its wholly-owned subsidiaries, CTI Balloons Limited, CTI Helium, Inc. and CTF International S.A. de C.V., its majority-owned subsidiaries CTI Mexico S.A. de C.V., Flexo Universal, S.A. de C.V. and CTI Europe gmbH, as well as the accounts of Venture Leasing S. A. de R. L. and Venture Leasing L.L.C (the “Company”). The last two entities have been consolidated as variable interest entities. All significant intercompany transactions and accounts have been eliminated in consolidation. The Company (i) designs, manufactures and distributes balloon products throughout the world and (ii) operates systems for the production, lamination, coating and printing of films used for food packaging and other commercial uses and for conversion of films to flexible packaging containers and other products.

Variable Interest Entities ("VIE'S"):

The determination of whether or not to consolidate a variable interest entity under U.S. GAAP requires a significant amount of judgment concerning the degree of control over an entity by its holders of variable interest. To make these judgments, management has conducted an analysis of the relationship of the holders of variable interest to each other, the design of the entity, the expected operations of the entity, which holder of variable interests is most "closely associated" to the entity and which holder of variable interests is the primary beneficiary required to consolidate the entity. Upon the occurrence of certain events, management reviews and reconsiders its previous conclusion regarding the status of an entity as a variable interest entity. Upon the adoption of amended accounting guidance applicable to variable interest entities on January 1, 2010, management continually reconsiders whether we are deemed to be a variable interest entity's primary beneficiary who consolidates such entity. The Company has two entities that have been consolidated as variable interest entities.

Use of estimates:

In preparing condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, management makes estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amount of revenue and expenses during the reporting period in the condensed consolidated financial statements and accompanying notes. Actual results may differ from those estimates. The Company’s significant estimates include reserves for doubtful accounts, reserves for the lower of cost or market of inventory, reserves for deferred tax assets and recovery value of goodwill.

Earnings per share:

Basic earnings per share is computed by dividing net income by the weighted average number of shares of common stock outstanding during each period.

Diluted earnings per share is computed by dividing the net income by the weighted average number of shares of common stock and equivalents (stock options and warrants), unless anti-dilutive, during each period.

As of March 31, 2011, shares to be issued upon the exercise of options aggregated 206,000. There are no longer any warrants to be exercised. As of March 31, 2010, shares to be issued upon the exercise of options and warrants were 191,858 and 343,030. The number of anti-dilutive shares (not included in the determination of earnings on a diluted basis) for the three months ended March 31, 2011 were 20,000, all of which were represented by options. The number of anti-dilutive shares (not included in the determination of earnings on a diluted basis) for the three months ended March 31, 2010 were 453,030 of which 110,000 were represented by options and 343,030 were represented by warrants.

New Accounting Pronouncements:

The Company's significant accounting policies are summarized in Note 2 of the Company's consolidated financial statements for the year ended December 31, 2010. There were no significant changes to these accounting policies during the three months ended March 31, 2011 and the Company does not expect that the adoption of other recent accounting pronouncements will have a material impact in its consolidated financial statements.

Note 2 - Stock-Based Compensation; Changes in Equity

We have adopted Financial Accounting Standards Board ("FASB") Accounting Standards Codification ("ASC") Topic 718 which requires all share-based payments to employees, including grants of employee stock options, to be recognized in the condensed consolidated financial statements based on their grant-date fair values.

We have applied the Black-Scholes model to value stock-based awards. That model incorporates various assumptions in the valuation of stock-based awards relating to the risk-free rate of interest to be applied, the estimated dividend yield and expected volatility of our common stock. The risk-free rate of interest is the related U.S. Treasury yield curve for periods within the expected term of the option at the time of grant. The dividend yield on our common stock is estimated to be 1.66%. The expected volatility is based on historical volatility of the Company's common stock.

The Company's net income for the three months ended March 31, 2011 and 2010 includes approximately $35,000 and $47,000, respectively of compensation costs related to share based payments. As of March 31, 2011 there is $246,000 of unrecognized compensation expense related to non-vested stock option grants and stock grants. We expect approximately $99,000 to be recognized over the remainder of 2011, $88,000 to be recognized during 2012, and $59,000 to be recognized during 2013.

As of March 31, 2011, the Company had four stock-based compensation plans pursuant to which stock options were, or may be, granted. The Plans provide for the award of options, which may either be incentive stock options ("ISOs") within the meaning of Section 422A of the Internal Revenue Code of 1986, as amended (the "Code") or non-qualified options ("NQOs") which are not subject to special tax treatment under the Code.

On April 12, 2001, the Board of Directors approved for adoption, effective December 27, 2001, the 2001 Stock Option Plan ("2001 Plan"). The 2001 Plan authorizes the grant of options to purchase up to an aggregate of 119,050, shares of the Company's Common Stock. As of March 31, 2011, 139,958 shares have been granted and were fully vested at the time of grant, 7,500 remain outstanding.

On April 24, 2002, the Board of Directors approved for adoption, effective October 12, 2002, the 2002 Stock Option Plan ("2002 Plan"). The 2002 Plan authorizes the grant of options to purchase up to an aggregate of 142,860 shares of the Company's Common Stock. As of March 31, 2011, 123,430 shares have been granted and were fully vested at the time of grant, 27,500 remain outstanding.

On April 30, 2007, the Board of Directors approved for adoption, effective October 1, 2007, the 2007 Stock Option Plan ("2007 Plan"). The 2007 Plan authorizes the grant of options to purchase up to an aggregate of 150,000 shares of the Company's Common Stock. As of March 31, 2011, 165,750 options had been granted and 89,500 remain outstanding.

On April 10, 2009, the Board of Directors approved for adoption, and on June 5, 2009, the shareholders of the Corporation approved, a 2009 Stock Incentive Plan ("2009 Plan"). The 2009 Plan authorizes the issuance of up to 250,000 shares of stock or options to purchase stock of the Company. As of March 31, 2011, 82,000 options had been granted and 81,500 remain outstanding.

A summary of the Company's stock option activity and related information is as follows:

	Shares under Option	Weighted Avgerage Exercise Price	Weighted Average Contractual Life	Aggregate Intrinsic Value
Balance at December 31, 2010	202,750	$ 4.28		
Granted	8,000	$ 5.96		
Cancelled	(4,250)	$ 6.12		
Exercised	(500)	$ 4.67		
Outstanding at March 31, 2011	206,000	$ 4.31	3.20	$231,976
Exercisable at March 31, 2011	107,875	$ 3.30	2.20	$181,726

During the three months ended March 31, 2011 there was no activity related to the Company's stock warrants.

A summary of the Company's stock option activity by grant date as of March 31, 2011 is as follows:

Options by		Options Outstanding			Options Vested
Grant Date	Shares	Wtd Avg	Remain. Life	Intrinsic Val	