

CSP INC /MA/
Form 10-Q
August 09, 2007

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

FORM 10-Q

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

For the Quarterly Period Ended June 30, 2007.

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

For the transition period from _____ to _____.

Commission File Number 0-10843

CSP Inc.
(Exact name of Registrant as specified in its Charter)

Massachusetts
(State of incorporation)

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

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

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

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Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer

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

As of August 1, 2007, the registrant had 3,815,276 of common stock issued and outstanding.

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

	June 30,	September 30,
	2007	2006
	(Unaudited)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 10,677	\$ 8,683
Short-term investments	3,370	2,173
Accounts receivable, net of allowances of \$134 and \$77	12,388	10,316
Inventories	9,476	7,407
Refundable income taxes	107	43
Deferred income taxes	998	1,361
Other current assets	2,128	1,632
Total current assets	39,144	31,615
Property, equipment and improvements, net	1,084	1,141
Other assets:		
Goodwill	2,779	2,779
Deferred income taxes	357	327
Cash surrender value of life insurance	1,900	2,185
Other assets	350	403
Total other assets	5,386	5,694
Total assets	\$ 45,614	\$ 38,450
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Accounts payable and accrued expenses	\$ 12,661	\$ 10,695
Pension and retirement plans	555	494
Income taxes payable	1,575	827
Deferred income taxes	606	—
Total current liabilities	15,397	12,016
Pension and retirement plans	7,810	7,283
Deferred income taxes	268	236
Total liabilities	23,475	19,535
Commitments and contingencies		
Shareholders' equity:		
Common stock, \$.01 par; authorized, 7,500 shares; issued 3,815 and 3,716 shares, respectively	38	37

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Additional paid-in capital	11,775	10,957
Retained earnings	13,302	11,187
Accumulated other comprehensive loss	(2,976)	(3,266)
Total shareholders' equity	22,139	18,915
Total liabilities and shareholders' equity	\$ 45,614	\$ 38,450

See accompanying notes to unaudited consolidated financial statements.

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

	For the three months ended		For the nine months ended	
	June 30, 2007	June 30, 2006	June 30, 2007	June 30, 2006
Sales:				
Product	\$ 21,871	\$ 14,468	\$ 54,929	\$ 41,342
Services	4,073	4,088	10,964	9,957
Total sales	25,944	18,556	65,893	51,299
Cost of sales:				
Product	16,837	12,588	42,217	33,388
Services	3,405	2,571	8,131	6,698
Total cost of sales	20,242	15,159	50,348	40,086
Gross profit	5,702	3,397	15,545	11,213
Operating expenses:				
Engineering and development	665	500	1,838	1,579
Selling, general and administrative	3,762	2,983	10,317	9,244
Total operating expenses	4,427	3,483	12,155	10,823
Operating income (loss)	1,275	(86)	3,390	390
Other income (expense):				
Foreign exchange gain (loss)	(1)	(3)	(1)	(5)
Other income (expense), net	333	71	503	309
Total other income (expense), net	332	68	502	304
Income (loss) before income taxes	1,607	(18)	3,892	694
Income tax expense	725	26	1,777	251
Net income (loss)	\$ 882	\$ (44)	\$ 2,115	\$ 443
Net income (loss) per share - basic	\$ 0.23	\$ (0.01)	\$ 0.56	\$ 0.12
Weighted average shares outstanding - basic	3,810	3,685	3,761	3,682
Net income (loss) per share - diluted	\$ 0.22	\$ (0.01)	\$ 0.54	\$ 0.12
Weighted average shares outstanding - diluted	3,967	3,685	3,926	3,791

See accompanying notes to unaudited consolidated financial statements

CSP INC. AND SUBSIDIARIES
UNAUDITED CONSOLIDATED STATEMENT OF SHAREHOLDERS' EQUITY
For the Nine Months Ended June 30, 2007
(Amounts in thousands)

	Shares	Amount	Additional Paid-in Capital	Retained Earnings	Accumulated other comprehensive income (loss)	Total Shareholders' Equity	Comprehensive income (loss)
Balance as of September 30, 2006	3,716	\$ 37	\$ 10,957	\$ 11,187	\$(3,266)	18,915	
Comprehensive income:							
Net income	—	—	—	2,115	—	2,115	\$ 2,115
Other comprehensive income (loss)							
Effect of foreign currency translation	—	—	—	—	290	290	290
Total Comprehensive income	—	—	—	—	—	—	—\$ 2,405
Exercise of stock options	70	1	362	—	—	363	
Stock-based compensation	—	—	257	—	—	257	
Issuance of shares under employee stock purchase plan	28	—	193	—	—	193	
Issuance of common stock	1	—	6	—	—	6	
Balance as of June 30, 2007	3,815	\$ 38	\$ 11,775	\$ 13,302	\$(2,976)	22,139	

See accompanying notes to unaudited consolidated financial statements

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

	For the nine months ended	
	June 30,	June 30,
	2007	2006
Cash flows from operating activities:		
Net income	\$ 2,115	\$ 443
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	486	410
Insurance Settlement Gain	(240)	—
Loss on disposal of property, net	1	5
Non-cash changes in accounts receivable	96	56
Non-cash compensation expense related to stock options	257	202
Deferred income taxes	994	53
Increase in cash surrender value of life insurance	—	(17)
Changes in operating assets and liabilities:		
Increase in accounts receivable	(1,823)	(4,340)
Increase in inventories	(1,945)	(1,445)
Increase in refundable income taxes	(60)	(12)
Increase in other current assets	145	(473)
Decrease in other assets	54	(198)
Increase in accounts payable and accrued expenses	1,629	5,503
Increase in pension and retirement plans	247	235
Increase in income taxes payable	730	155
Net cash provided by operating activities	2,686	577
Cash flows from investing activities:		
Purchases of available-for-sale securities	—	(31)
Purchases of held-to-maturity securities	(3,786)	(1,877)
Sales of available-for-sale securities	—	343
Maturities of held-to-maturity securities	2,589	2,073
Life insurance premiums paid	(48)	(91)
Purchases of property, equipment and improvements	(406)	(396)
Net cash provided by (used in) investing activities	(1,651)	21
Cash flows from financing activities:		
Proceeds from stock issued from the exercise of options	363	11
Proceeds from issuance of stock under employee stock purchase plan	193	158
Purchase of common stock	7	(110)
Net cash provided by financing activities	563	59
Effects of exchange rate changes on cash	396	430

Net increase in cash and cash equivalents	1,994	1,087
Cash and cash equivalents, beginning of period	8,683	9,724
Cash and cash equivalents, end of period	\$ 10,677	\$ 10,811
Supplementary Cash flow information:		
Cash paid for income taxes	\$ 104	\$ 91
Cash paid for interest	\$ 97	\$ 89

See accompanying notes to unaudited consolidated financial statements.

CSP INC. AND SUBSIDIARIES

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS THREE AND NINE MONTHS ENDED JUNE 30, 2007 AND 2006

Organization and Business

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

1. Basis of Presentation

The accompanying financial statements have been prepared by the Company, without audit, and reflect all adjustments which, in the opinion of management, are necessary for a fair statement of the results of the interim periods presented. All adjustments were of a normal recurring nature. Certain information and footnote disclosures normally included in the annual financial statements, which are prepared in accordance with accounting principles generally accepted in the United States of America, have been condensed or omitted. Accordingly, the Company believes that although the disclosures are adequate to make the information presented not misleading, the financial statements should be read in conjunction with the footnotes contained in the Company's Annual Report on Form 10-K for the fiscal year ended September 30, 2006.

2. New Accounting Pronouncements

In June 2006, the FASB issued Interpretation No. 48, "Accounting for Uncertainty in Income Taxes (as amended)—an interpretation of FASB Statement No. 109" ("FIN 48"). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements in accordance with SFAS No. 109, "Accounting for Income Taxes," and prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. We are in the process of analyzing the impact of FIN 48, which we are required to adopt by the first quarter of fiscal 2008.

In September 2006, the FASB issued SFAS No. 158, "*Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans—an amendment of FASB Statements No. 87, 88, 106, and 132(R)*" (SFAS 158), which requires recognition of the funded status of a benefit plan in the balance sheet. SFAS 158 also requires recognition, in other comprehensive income, of certain gains and losses that arise during the period but which are deferred under pension accounting rules. SFAS 158 also requires defined benefit plan assets and obligations to be measured as of the date of the employer's fiscal year-end. SFAS 158 provides recognition and disclosure elements that will be effective as of the end of fiscal years ending after December 15, 2006 (as of September 30, 2007 for the Company) and measurement date elements that will be effective for fiscal years ending after December 15, 2008 (as of September 30, 2009 for the Company). The Company is currently evaluating the recognition element of adopting SFAS 158. The measurement date element will not have an impact on the Company as the Company already measures the plan assets and obligations as of the end of its fiscal year.

3. Use of Estimates

The preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets

and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results may differ from those estimates under different assumptions or conditions.

4. Earnings Per Share of Common Stock

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

The reconciliation of the denominators of the basic and diluted net income (loss) per share computations for the Company's reported net income (loss) is as follows:

	For the Three Months Ended		For the Nine Months Ended	
	June 30, 2007	June 30, 2006	June 30, 2007	June 30, 2006
	(Amounts in thousands, except per share data)			
Net income (loss)	\$ 882	\$ (44)	\$ 2,115	\$ 443
Weighted average number of shares outstanding - basic	3,810	3,685	3,761	3,682
Incremental shares from the assumed exercise of stock options	157	—	165	109
Weighted average number of shares outstanding - diluted	3,967	3,685	3,926	3,791
Net income (loss) per share - basic	\$ 0.23	\$ (0.01)	\$ 0.56	\$ 0.12
Net income (loss) per share - diluted	\$ 0.22	\$ (0.01)	\$ 0.54	\$ 0.12

For the three and nine months ended June 30, 2007, options of 325 thousand and 339 thousand, respectively, were excluded from the diluted net income per share calculation because their impact would have been anti-dilutive. For the nine months ended June 30, 2006, options of 145 thousand, were excluded from the diluted net income per share calculation because their impact would have been anti-dilutive.

5. Inventories

Inventories consist of the following:

	June 30, 2007	September 30, 2006
	(Amounts in thousands)	
Raw materials	\$ 2,113	\$ 1,329
Work-in-progress	1,413	1,379
Finished goods	5,950	4,699
Total	\$ 9,476	\$ 7,407

6. Comprehensive Income (Loss)

The components of comprehensive income (loss) are as follows:

	For the Three Months Ended		For the Nine Months Ended	
	June 30, 2007	June 30, 2006	June 30, 2007	June 30, 2006
	(Amounts in thousands, except per share data)			
Net income (loss)	\$ 882	\$ (44)	\$ 2,115	\$ 443
Unrealized loss on available-for-sale securities	—	—	—	(45)

Effect of foreign currency translation	62	311	290	231
Comprehensive income	\$ 944	\$ 267	\$ 2,405	\$ 629

The components of Accumulated Other Comprehensive Income (Loss) are as follows:

	June 30, 2007	September 30, 2006
	(Amounts in thousands)	
Cumulative effect of foreign currency translation	\$ (1,066)	\$ (1,356)
Additional minimum pension liability	(1,910)	(1,910)
Accumulated Comprehensive income (loss)	\$ (2,976)	\$ (3,266)

7. Pension and Retirement Plans

In the United Kingdom and Germany, the Company provides defined benefit pension plans and defined contribution plans for the majority of its employees. Domestically, the Company also provides benefits through supplemental retirement plans to certain current and former employees. These supplemental plans provide benefits derived out of cash surrender values relating to current and former employee and officer life insurance policies, equal to the difference between the amounts that would have been payable under the defined benefit pension plans, in the absence of legislation limiting pension benefits and earnings that may be considered in calculating pension benefits, and the amounts actually payable under the defined benefit pension plans. Domestically, the Company provides for officer death benefits through post-retirement plans to certain officers.

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

The plan assets comprise a diversified mix of assets including corporate equity securities, government securities and corporate debt securities.

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

	For the Three Months Ended June 30					
	2007		2006			
	Foreign	U.S.	Total	Foreign	U.S.	Total
	(Amounts in thousands)					
Pension:						
Service cost	\$ 30	\$ 2	\$ 32	\$ 29	\$ 2	\$ 31
Interest cost	166	35	201	142	36	178
Expected return on plan assets	(122)	—	(122)	(99)	—	(99)
Amortization of:						
Prior service costs/(gains)	11	12	23	8	22	30
Net transition asset	(1)	—	(1)	(25)	—	(25)
Net periodic benefit cost	\$ 84	\$ 49	\$ 133	\$ 55	\$ 60	\$ 115
Post Retirement:						
Service cost	\$ —	\$ 14	\$ 14	\$ —	\$ 14	\$ 14
Interest cost	—	10	10	—	9	9
Expected return on plan assets	—	—	—	—	—	—