

MICROPAC INDUSTRIES INC  
Form 10-Q  
April 12, 2016

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 February 27, 2016

OR

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

Commission File Number 0-5109

MICROPAC INDUSTRIES, INC.

|   |                     |
|---|---------------------|
| <u>Delaware</u>                         | <u>75-1225149</u>   |
| (State of Incorporation)                | (IRS Employer       |
| <u>905 E. Walnut, Garland, Texas</u>    | Identification No.) |
| (Address of Principal Executive Office) | <u>75040</u>        |
|   | (Zip Code)          |

Registrant's Telephone Number, including Area Code (972) 272-3571

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 x 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 x No o

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):

Large accelerated filer o Accelerated filer o

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

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

On April 11, 2016 there were 2,578,315 shares of Common Stock, \$0.10 par value outstanding.

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MICROPAC INDUSTRIES, INC.

FORM 10-Q

February 27, 2016

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PART I - FINANCIAL INFORMATIONITEM 1. FINANCIAL STATEMENTSMICROPAC INDUSTRIES, INC.  
CONDENSED BALANCE SHEETS  
(Dollars in thousands)

## ASSETS

| CURRENT ASSETS   | <u>02/27/16</u><br>(Unaudited) | <u>11/30/15</u> |
|--|--------------------------------|-----------------|
| Cash and cash equivalents  | \$ 12,090                      | \$ 12,651       |
| Short-term investments   | 2,006                          | 2,004           |
| Receivables, net of allowance for doubtful accounts of<br>\$0 at February 27, 2016 and November 30, 2015 | 2,365                          | 2,360           |
| Inventories:   |                                |                 |
| Raw materials and supplies   | 3,889                          | 4,255           |
| Work-in process  | 2,874                          | 2,613           |
| Total inventories  | 6,763                          | 6,868           |
| Deferred income taxes  | 693                            | 693             |
| Prepaid expenses and other assets  | 143                            | 161             |
| Total current assets   | 24,060                         | 24,737          |
| <br>PROPERTY, PLANT AND EQUIPMENT, at cost:  |                                |                 |
| Land   | 80                             | 80              |
| Buildings  | 498                            | 498             |
| Facility improvements  | 1,109                          | 1,109           |
| Furniture and fixtures   | 719                            | 719             |
| Construction in process equipment  | 349                            | 347             |
| Machinery and equipment  | 8,430                          | 8,432           |
| Total property, plant, and equipment   | 11,185                         | 11,185          |
| Less accumulated depreciation  | (9,003 )                       | (8,929 )        |
| Net property, plant, and equipment   | 2,182                          | 2,256           |
| <br>Total assets   | \$ 26,242                      | \$ 26,993       |
| <br>LIABILITIES AND SHAREHOLDERS' EQUITY   |                                |                 |
| <br>CURRENT LIABILITIES:   |                                |                 |
| Accounts payable   | \$ 452                         | \$ 404          |
| Accrued compensation   | 410                            | 666             |
| Deferred revenue   | 2,720                          | 2,855           |
| Property Taxes   | 23                             | 90              |
| Income taxes payable   | 1                              | 109             |
| Other accrued liabilities  | 93                             | 74              |
| Total current liabilities  | 3,699                          | 4,198           |

|  |           |           |
|--|-----------|-----------|
| DEFERRED INCOME TAXES  | 360       | 360       |
| SHAREHOLDERS' EQUITY   |           |           |
| Common stock, (\$.10 par value), authorized 10,000,000<br>shares, 3,078,315 issued and 2,578,315 outstanding at<br>February 27, 2016 and November 30, 2015 | 308       | 308       |
| Additional paid-in capital   | 885       | 885       |
| Treasury stock, 500,000 shares, at cost  | (1,250 )  | (1,250 )  |
| Retained earnings  | 22,240    | 22,492    |
| Total shareholders' equity   | 22,183    | 22,435    |
| Total liabilities and shareholders' equity   | \$ 26,242 | \$ 26,993 |

See accompanying notes to financial statements.

MICROPAC INDUSTRIES, INC.  
CONDENSED STATEMENTS OF OPERATIONS  
(Dollars in thousands except share data)  
(Unaudited)

|   | <u>Three months ended</u> |                 |
|---|---------------------------|-----------------|
|   | <u>02/27/16</u>           | <u>02/28/15</u> |
| NET SALES                                     | \$4,205                   | \$4,786         |
| COST AND EXPENSES:                            |                           |                 |
| Cost of goods sold                            | (2,894 )                  | (2,850 )        |
| Research and development                      | (307 )                    | (568 )          |
| Selling, general & administrative expenses    | (1,003 )                  | (1,040 )        |
| Total cost and expenses                       | (4,204 )                  | (4,458 )        |
| OPERATING INCOME                              | 1                         | 328             |
| Other income                                  | 7                         | 2               |
| Expense, net                                  | -                         | (2 )            |
| INCOME BEFORE TAXES                           | 8                         | 328             |
| Provision for taxes                           | (3 )                      | (118 )          |
| NET INCOME                                    | \$5                       | \$210           |
| NET INCOME PER SHARE, BASIC AND DILUTED       | \$0.00                    | \$0.08          |
| DIVIDENDS PER SHARE                           | \$0.10                    | \$0.10          |
| WEIGHTED AVERAGE OF SHARES, basic and diluted | 2,578,315                 | 2,578,315       |

See accompanying notes to financial statements.



MICROPAC INDUSTRIES, INC.  
 CONDENSED STATEMENTS OF CASH FLOWS  
 (Dollars in thousands)  
 (Unaudited)

|  | <u>Three months</u><br><u>ended</u> |                |
|--|-------------------------------------|----------------|
|  | <u>2/27/16</u>                      | <u>2/28/15</u> |
| <b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>   |                                     |                |
| Net income   | \$5                                 | \$210          |
| Adjustments to reconcile net income to<br>net cash provided by (used in) operating activities: |                                     |                |
| Depreciation and amortization  | 74                                  | 77             |
| Deferred taxes   | -                                   | 19             |
| Changes in certain current assets and liabilities:   |                                     |                |
| Accounts receivable  | (5 )                                | (1,003 )       |
| Inventories  | 105                                 | 151            |
| Prepaid expenses and other current assets  | 18                                  | 72             |
| Accounts payable   | 48                                  | (53 )          |
| Accrued compensation   | (256 )                              | (175 )         |
| Deferred revenue   | (135 )                              | 3,159          |
| Other accrued liabilities  | (48 )                               | (7 )           |
| Income taxes payable   | (108 )                              | 55             |
| Net cash provided by (used in) operating activities  | (302 )                              | 2,505          |
| <b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>   |                                     |                |
| Sale of short term investments   | 2,004                               | 2,009          |
| Purchase of short term investments   | (2,006 )                            | (2,001 )       |
| Additions to property, plant and equipment   | 1                                   | (37 )          |
| Net cash used in investing activities  | (1 )                                | (29 )          |
| <b>CASH FLOWS FROM FINANCING ACTIVITIES</b>  |                                     |                |
| Cash dividend  | (258 )                              | (258 )         |
| Net cash used in financing activities  | (258 )                              | (258 )         |
| Net change in cash and cash equivalents  | (561 )                              | 2,218          |
| Cash and cash equivalents at beginning of period   | 12,651                              | 9,994          |
| Cash and cash equivalents at end of period   | \$ 12,090                           | \$ 12,212      |
| <b>Supplemental Cash Flow Disclosure:</b>  |                                     |                |
| Cash paid for income taxes   | \$ 110                              | \$ -           |



See accompanying notes to financial statements.

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MICROPAC INDUSTRIES, iNC.  
NOTES TO CONDENSED FINANCIAL STATEMENTS  
(Unaudited)

Note 1 BASIS OF PRESENTATION

Business Description

Micropac Industries, Inc. (the "Company"), a Delaware corporation, manufactures and distributes various types of hybrid microelectronic circuits, solid state relays, power controllers, and optoelectronic components and assemblies. The Company's products are used as components in a broad range of military, space and industrial systems, including aircraft instrumentation and navigation systems, power supplies, electronic controls, computers, medical devices, and high-temperature (200° C) products.

In the opinion of management, the unaudited financial statements include all adjustments (consisting of only normal, recurring adjustments) necessary to present fairly the financial position as of February 27, 2016, the results of operations for the three months ended February 27, 2016 and February 28, 2015, and the cash flows for the three months ended February 27, 2016 and February 28, 2015. Unaudited financial statements are prepared on a basis substantially consistent with those audited for the year ended November 30, 2015. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles in the United States have been condensed or omitted pursuant to the rules and regulations promulgated by the Securities and Exchange Commission. The Company's fiscal year ends on the last day of November. The quarterly results end on the last Saturday of the quarter.

Note 2 SIGNIFICANT ACCOUNTING POLICIES

Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles 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 sales and expenses during the reporting period. Actual results could differ from those estimates.

Revenue Recognition

Sales are recorded as shipments are made based upon contract prices. Any losses anticipated on fixed price contracts are provided for currently. Sales are recorded net of sales returns, allowances and discounts.

The Company recognizes sales when four basic criteria must be met: (1) persuasive evidence of an arrangement exists; (2) shipment has occurred or services have been rendered; (3) the fee is fixed and determinable; and (4) collectibility is reasonably assured.

Deferred revenue represents prepayments from customers and will be recognized as sales when the products are shipped per the terms of the contract.

Short-Term Investments

The Company has \$2,006,000 in short term investments at February 27, 2016. Short-term investments consist of certificates of deposits with initial maturities greater than 90 days. These investments are reported at historical cost,

which approximates fair value. All highly liquid investments with initial maturities of 90 days or less are classified as cash equivalents. All short-term investments are securities which the Company has the ability and intent to hold to maturity and mature within one year.

Inventories

Inventories are stated at lower of cost or market value and include material, labor and manufacturing overhead. All inventories are valued using the FIFO (first-in, first-out) method of inventory valuation. The Company determines the need to write inventory down below its cost via an analysis based on the usage of inventory over a three year period and projected usage based on current backlog.

Income Taxes

The Company accounts for income taxes using the asset and liability method. Under this method the Company records deferred income taxes for the temporary differences between the financial reporting basis and the tax basis of assets and liabilities at enacted tax rates expected to be in effect when such amounts are realized or settled. The resulting deferred tax liabilities and assets are adjusted to reflect changes in tax law or rates in the period that includes the enactment date.

Property, Plant, and Equipment

Property, plant, and equipment are carried at cost, and depreciation is provided using the straight-line method at rates based upon the following estimated useful lives (in years) of the assets:

|                         |      |
|-------------------------|------|
| Buildings               | 15   |
| Facility improvements   | 8-15 |
| Machinery and equipment | 5-10 |
| Furniture and fixtures  | 5-8  |

The Company assesses long-lived assets for when events or circumstances indicate that an asset may be impaired. The estimated future undiscounted cash flows associated with the asset are compared to the asset's net book value to determine if a write down to market value less cost to sell is required.

Repairs and maintenance are expensed as incurred. Improvements which extend the useful life of property, plant, and equipment are capitalized.

Research and Development Costs

Costs for the design and development of new products and processes are expensed as incurred.

Note 3 NEW ACCOUNTING PRONOUNCEMENTS

On May 28, 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers, which requires an entity to recognize the amount of revenue to which it expects to be entitled for the transfer of promised goods and services to customers. The ASU will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. The standard permits the use of either the retrospective or cumulative effect transition method. The Company is evaluating the effect that ASU 2014-09 will have on its consolidated financial statements and related disclosures. On July 9, 2015 the FASB agreed to defer the effective date to annual reporting periods beginning after December 15, 2017 and the interim periods within that year. The Company has not yet selected a transition method nor has it determined the effect of the standard on its ongoing financial reporting.

Note 4 FAIR VALUE MEASUREMENT

The Company had no financial assets or liabilities measured at fair value on a recurring basis as of February 27, 2016 and November 30, 2015. The fair value of financial instruments such as cash and cash equivalents, short term investments, accounts receivable, and accounts payable approximate their carrying amount based on the short maturity of these instruments. There were no nonfinancial assets measured at fair value on a nonrecurring basis at February 27, 2016 and November 30, 2015.

Note 5 COMMITMENTS

On January 23, 2015, the Company renewed the Loan Agreement with a Texas banking institution. The Loan Agreement provides for revolving credit loans, in amounts not to exceed a total principal balance of \$6,000,000, and specific advance loans for acquisitions with an aggregate amount not to exceed \$7,500,000 in a single advance or in multiple advances. The Loan Agreement also contains financial covenants to maintain at all times including (i) minimum working capital of not less than \$4,000,000, (ii) a ratio of senior funded debt, minus the Company's balance sheet cash on hand to the extent in excess of \$2,000,000 to EBITDA of not more than 3.0 to 1.0, and (iii) a ratio of free cash flow to debt service of not less than 1.2 to 1.0. The Company has not, to date, drawn any amounts under the loan agreement or the revolving line of credit and is currently in compliance with the financial covenants.

#### Note 6 EARNINGS PER COMMON SHARE

Basic and diluted earnings per share are computed based upon the weighted average number of shares outstanding during the respective periods. Diluted earnings per share gives effect to all dilutive potential common shares. For the three months ended February 27, 2016 and February 28, 2015, the Company had no dilutive potential common stock.

Note 7 SHAREHOLDERS' EQUITY

On December 16, 2014, the Board of Directors of Micropac Industries, Inc. approved the payment of a special dividend of \$0.10 per share for shareholders of record as of January 12, 2015. The dividend was paid to shareholders on February 10, 2015.

On December 15, 2015, the Board of Directors of Micropac Industries, Inc. approved the payment of a special dividend of \$0.10 per share for shareholders of record as of January 12, 2016. The dividend was paid to shareholders on February 11, 2016.

MICROPAC INDUSTRIES, INC.  
(Unaudited)

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

Business

Micropac Industries, Inc. (the "Company"), a Delaware corporation, manufactures and distributes various types of hybrid microelectronic circuits, solid state relays, power management products, and optoelectronic components and assemblies. The Company's products are used as components in a broad range of military, space and industrial systems, including aircraft instrumentation and navigation systems, power supplies, electronic controls, computers, medical devices, and high-temperature (200° C) products. The Company's products are either custom (being application specific circuits designed and manufactured to meet the particular requirements of a single customer) or standard, proprietary components such as catalog items.

The Company's facilities are certified and qualified by Defense Logistics Agency (DLA) to MIL-PRF-38534 (class K-space level), MIL-PRF-19500 JANS (space level), and MIL-PRF-28750 (class K-space level) and is certified to ISO 9001-2002. Micropac is a NASA core supplier, and is registered to AS9100-Aerospace Industry standard for supplier certification. The Company has UL approval on the new isolated solid state industrial power controllers.

The Company's core technology is the packaging and interconnecting of miniature electronic components, utilizing thick film substrates, forming microelectronics circuits. Other technologies include light emitting and light sensitive materials and products, including light emitting diodes and silicon phototransistors used in the Company's optoelectronic components and assemblies

Results of Operations

|  | <u>Three months ended</u>  |             |          |
|--|----------------------------|-------------|----------|
|  | <u>2/27/2016/2/28/2015</u> |             |          |
| NET SALES                                  | 100.0%                     | 100.0       | %        |
| COST AND EXPENSES:                         |                            |             |          |
| Cost of Goods Sold                         | 68.9 %                     | 59.5        | %        |
| Research and development                   | 7.3 %                      | 11.9        | %        |
| Selling, general & administrative expenses | <u>23.8 %</u>              | <u>21.7</u> | <u>%</u> |
| Total cost and expenses                    | 100.0%                     | 93.1        | %        |
| OPERATING INCOME                           | 0.0 %                      | 6.9         | %        |
| Other income                               | 0.2 %                      | -           |          |
| INCOME BEFORE TAXES                        | 0.2 %                      | 6.9         | %        |
| Provision for taxes                        | 0.1 %                      | 2.5         | %        |
| NET INCOME                                 | 0.1 %                      | 4.4         | %        |

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Sales for the first quarter ended February 27, 2016 totaled \$4,205,000. Sales for the first quarter decreased 12.1% or \$581,000 below sales for the first quarter of 2015 with a decrease in various standard optocouplers products. Sales were 18% in the commercial market, 67% in the military market, and 15% in the space market in the first quarter of 2016 compared to 15% in the commercial market, 72% in the military market, and 13% in the space market for the same period of 2015.

Two customers accounted for 11% and 10% of the Company's sales for the first quarter of 2016 while one customer accounted for 17% of the Company's sales for the first quarter of 2015.



Cost of goods sold for the first quarter of 2016 and 2015 totaled 68.9% and 59.5% of net sales, respectively. Cost of goods sold increased \$44,000 in the first quarter of 2016 as compared to 2015 due to product mix and the decrease in various standard optocoupler product sales.

Research and development cost decreased \$261,000 for the first quarter of 2016 compared to the same period of 2015. The research and development expenditures were associated with the continued development of power management products, high voltage optocouplers and process automation improvements.

Selling, general and administrative expenses for the first quarter of 2016 totaled 23.8% of net sales, compared to 21.7% for the same period in 2015. Selling, general and administrative expenses decreased \$37,000 in the first quarter of 2016 as compared to 2015.

Provisions for taxes decreased \$116,000 for the first quarter of 2016 compared to the same period in 2015. The estimated effective tax rate was 32% for the first quarter of 2016 and 36% for the same period of 2015.

Net income for the first quarter of 2016 was \$5,000, a decrease of \$205,000 from the first quarter of 2015.

### Liquidity and Capital Resources

Cash and cash equivalents totaled \$12,090,000 as of February 27, 2016 compared to \$12,651,000 on November 30, 2015, a decrease of \$561,000. The decrease in cash and cash equivalents is attributable to \$286,000 cash used in operations, a payment of a cash dividend of \$258,000, net payments for short-term investment of \$2,000 and the investment of \$14,000 in equipment.

In addition to cash on hand, the Company also has the ability to borrow under a loan agreement as discussed in note 5 to the condensed financial statements.

### Outlook

New orders for the first quarter of 2016 totaled \$2,837,000 compared to \$6,642,000 for the comparable period of 2015. Backlog totaled \$17,558,000 on February 27, 2016 compared to \$22,949,000 as of February 28, 2015 and \$18,925,000 on November 30, 2015. The majority of the backlog is expected to be completed and shipped in the next twelve months.

The Company cannot assure that the results of operations for the interim period presented are indicative of total results for the entire year due to fluctuations in customer delivery schedules, or other factors over which the Company has no control.

### Cautionary Statement

This Form 10-Q contains forward-looking statements that are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Actual results could differ materially. Investors are warned that forward-looking statements involve risks and unknown factors including, but not limited to, customer cancellation or rescheduling of orders, problems affecting delivery of vendor-supplied raw materials and components, unanticipated manufacturing problems and availability of direct labor resources.

The Company produces silicon phototransistors and light emitting diode die for use in certain military, standard and custom products. Fabrication efforts sometimes may not result in successful results, limiting the availability of these components. Competitors offer commercial level alternatives and our customers may purchase our competitors' products if the Company is not able to manufacture the products using these technologies to meet the customer

demands. Approximately \$1,800,000 of the Company's backlog is dependent on these semiconductors.

The Company disclaims any responsibility to update the forward-looking statements contained herein, except as may be required by law.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Not applicable

ITEM 4. CONTROLS AND PROCEDURES

(a) Evaluation of disclosure controls and procedures.

The Chief Executive Officer and Chief Financial Officer of the Company evaluated the Company's disclosure controls and procedures (as defined in Exchange Act Rule 13a-15) as of February 27, 2016 and, based on this evaluation, concluded that the Company's disclosure controls and procedures are functioning in an effective manner to ensure that the information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act, is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms.

(b) Changes in internal controls.

There has been no change in the Company's internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting during the three month period ended February 27, 2016.

## PART II - OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

The Company is not involved in any material current or pending legal proceedings.

### ITEM 1A RISK FACTORS

Information about risk factors for the three months ended February 27, 2016 does not differ materially from that set forth in Part I, Item 1A, of our Annual Report on Form 10-K for the year ended November 30, 2015.

### ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

None

### ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None

### ITEM 4. MINE SAFETY DISCLOSURE

Not Applicable

### ITEM 5. OTHER INFORMATION

None

### ITEM 6. EXHIBITS

(a) Exhibits

31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certification of Chief Accounting Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1 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.

32.2 Certification of Chief Accounting Officer pursuant to 18 U. S. C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley act of 2002.



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 duly authorized.

MICROPAC INDUSTRIES, INC.

April 12, 2016 /s/ Mark King

Date Mark King  
Chief Executive Officer

April 12, 2016 /s/ Patrick Cefalu

Date Patrick Cefalu  
Chief Financial Officer

