

Proto Labs Inc
Form 10-Q
July 25, 2012
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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, 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: 001-35435

Proto Labs, Inc.

(Exact name of registrant as specified in its charter)

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Minnesota
(State or other jurisdiction of
incorporation or organization)
5540 Pioneer Creek Drive
Maple Plain, Minnesota
(Address of principal executive offices)

41-1939628
(I.R.S. Employer
Identification No.)
55359
(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: 23,935,578 shares of Common Stock, par value \$0.001 per share, were outstanding at July 16, 2012.

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Proto Labs, Inc.

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Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****Proto Labs, Inc.****Consolidated Balance Sheets****(In thousands, except share and per share amounts)**

	June 30, 2012 (Unaudited)	December 31, 2011
Assets		
Current assets		
Cash and cash equivalents	\$ 44,386	\$ 8,135
Short-term marketable securities	14,269	250
Accounts receivable, net of allowance for doubtful accounts of \$134 and \$97 as of June 30, 2012 and December 31, 2011, respectively	13,717	11,533
Inventory	3,986	3,797
Prepaid expenses and other current assets	3,529	3,430
Deferred tax assets	932	932
Total current assets	80,819	28,077
Property and equipment, net	44,083	34,249
Long-term marketable securities	20,073	
Total assets	\$ 144,975	\$ 62,326
Liabilities, redeemable convertible preferred stock, redeemable common stock and shareholders equity (deficit)		
Current liabilities		
Accounts payable	\$ 4,055	\$ 4,431
Accrued compensation	3,719	4,767
Accrued liabilities and other	725	318
Income taxes payable	690	33
Current portion of long-term debt obligations	378	390
Total current liabilities	9,567	9,939
Deferred tax liability	4,252	4,252
Long-term debt obligations	432	613
Other	815	871
Redeemable convertible stock		
Redeemable convertible preferred stock, \$0.001 par value, authorized, issued and outstanding 0 and 427,985 shares as of June 30, 2012 and December 31, 2011, respectively		66,075
Redeemable common stock, \$0.001 par value, issued and outstanding 0 and 3,189,648 shares as of June 30, 2012 and December 31, 2011, respectively		819
Shareholders' equity (deficit)		
Preferred stock, \$0.001 par value, authorized 10,000,000 and 0 shares; issued and outstanding 0 shares as of June 30, 2012 and December 31, 2011, respectively		
Common stock, \$0.001 par value, authorized 150,000,000 shares; issued and outstanding 23,935,578 and 9,706,270 shares as of June 30, 2012 and December 31, 2011, respectively	24	10
Additional paid in capital	134,007	8,229
Accumulated equity (deficit)	(3,527)	(27,744)

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Accumulated other comprehensive income (loss)	(595)	(738)
Total shareholders' equity (deficit)	129,909	(20,243)
Total liabilities, redeemable convertible preferred stock, redeemable common stock and shareholders' equity (deficit)	\$ 144,975	\$ 62,326

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

Table of Contents**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,	
	2012	2011	2012	2011
Statements of Operations:				
Revenue	\$ 29,951	\$ 24,052	\$ 59,921	\$ 46,387
Cost of revenue	12,239	9,517	24,482	17,946
Gross profit	17,712	14,535	35,439	28,441
Operating expenses				
Marketing and sales	4,557	3,924	8,998	7,139
Research and development	2,401	1,223	4,061	2,335
General and administrative	3,288	2,753	7,276	5,259
Total operating expenses	10,246	7,900	20,335	14,733
Income from operations	7,466	6,635	15,104	13,708
Other income (expense), net	173	78	(404)	(3)
Income before income taxes	7,639	6,713	14,700	13,705
Provision for income taxes	2,493	2,182	4,772	4,451
Net income	5,146	4,531	9,928	9,254
Less: dividends on redeemable preferred stock		(1,042)		(2,073)
Less: undistributed earnings allocated to preferred shareholders		(1,160)		(2,419)
Net income attributable to common shareholders	\$ 5,146	\$ 2,329	\$ 9,928	\$ 4,762
Net income per share:				
Basic	\$ 0.22	\$ 0.19	\$ 0.44	\$ 0.40
Diluted	\$ 0.20	\$ 0.17	\$ 0.42	\$ 0.37
Shares used to compute net income per share:				
Basic	23,929,886	12,007,674	22,432,415	12,013,876
Diluted	25,280,835	13,364,610	23,743,122	12,966,086
Comprehensive income	\$ 4,831	\$ 4,415	\$ 10,071	\$ 9,280

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

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

	Six Months Ended June 30,	
	2012	2011
Operating activities		
Net income	\$ 9,928	\$ 9,254
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	2,768	1,882
Stock-based compensation expense	1,620	411
Changes in operating assets and liabilities:		
Accounts receivable	(2,268)	(3,083)
Inventories	(189)	(375)
Prepaid expenses and other	27	236
Income taxes	660	(6)
Accounts payable	(363)	593
Accrued liabilities and other	(705)	1,525
Net cash provided by operating activities	11,478	10,437
Investing activities		
Purchases of property and equipment	(12,664)	(6,350)
Purchases of marketable securities	(34,342)	
Proceeds from sale of marketable securities	250	500
Net cash used in investing activities	(46,756)	(5,850)
Financing activities		
Proceeds from initial public offering, net of offering costs	71,530	
Proceeds from issuance of debt		637
Payments on debt	(191)	(3,885)
Proceeds from exercises of warrants and stock options	37	547
Net cash provided by (used in) financing activities	71,376	(2,701)
Effect of exchange rate changes on cash and cash equivalents	153	14
Net increase in cash and cash equivalents	36,251	1,900
Cash and cash equivalents, beginning of period	8,135	6,101
Cash and cash equivalents, end of period	\$ 44,386	\$ 8,001

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

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Proto Labs, Inc.

Notes to Consolidated Financial Statements

(Unaudited)

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.

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 prospectus filed on February 27, 2012 with the SEC pursuant to Rule 424(b)(4) of the Securities Act of 1933.

The accompanying Consolidated Balance Sheet as of December 31, 2011 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 prospectus filed on February 27, 2012 as referenced above.

On February 21, 2012, the Company executed a 14-for-1 forward stock split of the Company's common stock. The consolidated financial statements for all periods and dates presented give retroactive effect to the stock split.

Note 2 Recent Accounting Pronouncements

In May 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2011-04, *Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRS* (ASU 2011-04). This accounting update generally aligns the principles for fair value measurements and the related disclosure requirements under U.S. GAAP and International Financial Reporting Standards (IFRS). From a U.S. GAAP perspective, the amendments are largely clarifications, but some could have a significant effect on certain companies. A number of new disclosures also are required. Except for certain disclosures, the guidance applies to public and nonpublic companies and is to be applied prospectively. For public and nonpublic companies, the amendments are effective during interim and annual periods beginning after December 15, 2011. The Company adopted this accounting guidance effective January 1, 2012. The adoption of ASU 2011-04 did not result in a material impact to the Company's financial statements.

In June 2011, the FASB issued ASU 2011-05, *Presentation of Comprehensive Income* (ASU 2011-05). This accounting update requires entities to present items of net income and other comprehensive income either in a single continuous statement, or in separate, but consecutive, statements of net income and other comprehensive income. The new requirements do not change which components of comprehensive income are recognized in net income or other comprehensive income, or when an item of other comprehensive income must be reclassified to net income. However, the current option under existing standards to report other comprehensive income and its components in the statement of changes in equity is eliminated. In December 2011, the FASB issued ASU 2011-12, *Deferral of the Effective Date for Amendments to the Presentation of Reclassifications of Items Out of Accumulated Other Comprehensive Income in Accounting Standards Update No. 2011-05* (ASU 2011-12). The updated guidance defers the requirement in ASU 2011-05 to present on the face of the financial statements the effects of reclassifications out of accumulated other comprehensive income on the components of net income and other comprehensive income. The amendments apply to public and nonpublic companies and are to be applied retrospectively. For public entities, the amendments are effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. The Company adopted this accounting guidance effective January 1, 2012 and has presented net income and comprehensive income in a single continuous statement in this report. The adoption of ASU 2011-05 and ASU 2011-12 did not result in a material impact to the Company's financial statements.

Table of Contents**Proto Labs, Inc.****Notes to Consolidated Financial Statements****(Unaudited)****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 the 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 and other stock-based 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,		Six Months Ended June 30,	
	2012	2011	2012	2011
Net Income	\$ 5,146	\$ 4,531	\$ 9,928	\$ 9,254
Less: dividends on redeemable convertible preferred stock		(1,042)		(2,073)
Less: undistributed earnings allocated to preferred shareholders		(1,160)		(2,419)
Net income attributable to common shareholders	\$ 5,146	\$ 2,329	\$ 9,928	\$ 4,762
Basic weighted-average shares outstanding:	23,929,886	12,007,674	22,432,415	12,013,876
Effect of dilutive securities:				
Employee stock options, warrants and other	1,350,949	1,356,936	1,310,707	952,210
Diluted weighted-average shares outstanding:	25,280,835	13,364,610	23,743,122	12,966,086
Net income per share attributable to common shareholders:				
Basic	\$ 0.22	\$ 0.19	\$ 0.44	\$ 0.40
Diluted	\$ 0.20	\$ 0.17	\$ 0.42	\$ 0.37

Weighted-average diluted shares for the three and six month periods ended June 30, 2011 excludes redeemable convertible preferred stock as it was anti-dilutive for the periods.

Table of Contents**Proto Labs, Inc.****Notes to Consolidated Financial Statements****(Unaudited)**

The following table sets forth the calculation of unaudited pro forma basic and diluted net income per share which gives effect to the conversion of all outstanding shares of redeemable convertible preferred stock as if the conversion had occurred on January 1, 2011:

(in thousands, except share and per share amounts)	Three Months Ended June 30,		Six Months Ended June 30,	
	2012	2011	2012	2011
Net income attributable to common shareholders, as reported	\$ 5,146	\$ 2,329	\$ 9,928	\$ 4,762
Dividends on redeemable convertible preferred stock		1,042		2,073
Undistributed earnings allocated to preferred shareholders		1,160		2,419
Pro forma net income	\$ 5,146	\$ 4,531	\$ 9,928	\$ 9,254
Basic weighted-average shares outstanding, as reported	23,929,886	12,007,674	22,432,415	12,013,876
Add: common shares from conversion of redeemable convertible preferred shares		5,991,790		5,991,790
Pro forma basic weighted-average shares outstanding	23,929,886	17,999,464	22,432,415	18,005,666
Effect of dilutive securities:				
Employee stock options, warrants and other	1,350,949	1,356,936	1,310,707	952,210
Pro forma diluted weighted-average shares outstanding:	25,280,835	19,356,400	23,743,122	18,957,876
Pro forma net income per share attributable to common shareholders:				
Basic	\$ 0.22	\$ 0.25	\$ 0.44	\$ 0.51
Diluted	\$ 0.20	\$ 0.23	\$ 0.42	\$ 0.49

Note 4 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, 2012	December 31, 2011
Raw materials	\$ 3,738	\$ 3,463
Work in process	333	418

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Total Inventory	4,071	3,881
Allowance for obsolescence	(85)	(84)
Inventory, net of allowance	\$ 3,986	\$ 3,797

Note 5 Marketable Securities

During the three months ended June 30, 2012, the Company invested a portion of its cash in various marketable securities. The Company invests in agency, municipal and corporate bonds, and commercial paper and other 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. The following is a summary of the amounts recorded on the Consolidated Balance Sheet for marketable securities (current and non-current) as of June 30, 2012:

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(in thousands)	Amortized Cost	June 30, 2012 Unrealized Losses	Fair Value
U.S. government agency securities	\$ 4,011	\$	\$ 4,011
Corporate debt securities	3,338	(3)	3,335
Commercial paper	1,999	(1)	1,998
U.S. municipal securities	2,937		2,937
Certificates of deposit/time deposits	1,984	(3)	1,981
 Current marketable securities	 14,269	 (7)	 14,262
U.S. government agency securities	14,013	(7)	14,006
Corporate debt securities	5,056	(11)	5,045
U.S. municipal securities	1,004	(2)	1,002
 Non-current marketable securities	 20,073	 (20)	 20,053
 Total marketable securities	 \$ 34,342	 \$ (27)	 \$ 34,315

Fair values for the U.S. municipal and corporate debt securities are primarily determined based on quoted market prices (Level 1). Fair values for the 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 to be temporary in nature. The Company intends, and has the ability, 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.

Note 6 Fair Value Measurements

Accounting Standards Codification (ASC) 820, *Fair Value Measurement* (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

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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 as of June 30, 2012 consist of money market mutual funds. The Company's short-term marketable securities measured at fair value as of December 31, 2011 consisted of domestic certificates of deposits at various banks and treasury notes. The Company determines the fair value of these investments using Level I inputs.

A summary of financial assets as of June 30, 2012 and December 31, 2011 measured at fair value on a recurring basis follows:

(in thousands)	June 30, 2012			December 31, 2011		
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Financial Assets:						
Cash and cash equivalents						
Money market mutual fund	\$ 30,531	\$	\$	\$	\$	\$
Short-term marketable securities						
Certificates of deposit and treasury notes				250		
Total	\$ 30,531	\$	\$	\$ 250	\$	\$

Note 7 Shareholders' Equity**Initial Public Offering**

In February 2012, the Company issued 4.9 million shares of common stock (including the exercise of the underwriters' over-allotment shares) in conjunction with its initial public offering (IPO). The public offering price of the shares sold in the offering was \$16.00 per share. The total gross proceeds from the IPO to the Company were \$79.1 million. After deducting underwriting discounts and commissions and offering expenses payable by the Company, the aggregate net proceeds received by the Company totaled approximately \$71.5 million. As of June 30, 2012, all offering costs have been recorded.

Immediately prior to the consummation of the IPO, all outstanding shares of redeemable convertible preferred stock and redeemable common stock were converted into shares of common stock. Shares of redeemable convertible preferred stock were converted into 5,991,790 shares of common stock. All previously accrued dividends on the preferred stock were released back into retained earnings. Shares of redeemable common stock were converted into 3,189,648 shares of common stock. Refer to the tables below for additional information regarding the conversion.

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The following tables present the shares authorized and issued and outstanding as of the periods presented, as well as equity transactions during the six months ended June 30, 2012 (in thousands, except share data):

	June 30, 2012		December 31, 2011	
	Shares Authorized	Shares Issued and Outstanding	Shares Authorized	Shares Issued and Outstanding
Redeemable stock:				
Redeemable convertible preferred stock, \$0.001 par value			427,985	427,985
Redeemable common stock, \$0.001 par value			3,189,648	3,189,648
Shareholders' equity:				
Preferred stock, \$0.001 par value	10,000,000			
Common stock, \$0.001 par value	150,000,000	23,935,578	150,000,000	9,706,270

	Common Stock		Additional Paid-In	Accumulated	Accumulated Other Comprehensive Income (Loss)	Total
	Shares	Amount	Capital	Deficit		
Balance at December 31, 2011	9,706,270					