

ADVANCED ENERGY INDUSTRIES INC

FORM 10-Q (Quarterly Report)

Filed 11/13/1996 For Period Ending 9/30/1996

Address	1625 SHARP POINT DR FT COLLINS, Colorado 80525
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CIK	0000927003
Industry	Electronic Instr. & Controls
Sector	Technology
Fiscal Year	12/31

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 September 30, 1996.

**[] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
AND EXCHANGE ACT OF 1934.**

For the transition period from _____ to _____.

Commission file number: 0-26966

ADVANCED ENERGY INDUSTRIES, INC.

(Exact name of registrant as specified in its charter)

DELAWARE

84-0846841

(State or other jurisdiction of
incorporation or organization)

(I.R.S. Employer Identification No.)

1625 SHARP POINT DRIVE, FORT COLLINS, CO

80525

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code: (970) 221-4670

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 and 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__.

As of September 30, 1996, there were 21,251,192 shares of the Registrant's Common Stock, par value \$0.001 per share, outstanding.

ADVANCED ENERGY INDUSTRIES, INC.
FORM 10-Q

INDEX

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

Consolidated Balance Sheets-
September 30, 1996 and December 31, 1995 3

Consolidated Statements of Operations-
Three months and nine months ended September 30, 1996 and 1995 4

Consolidated Statements of Cash Flows-
Nine months ended September 30, 1996 and 1995 5

Notes to consolidated financial statements 6

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL
CONDITION AND RESULTS OF OPERATIONS 8

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS 14

ITEM 2. CHANGES IN SECURITIES 14

ITEM 3. DEFAULTS UPON SENIOR SECURITIES 14

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS 14

ITEM 5. OTHER INFORMATION 14

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K 14

PART I FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS AND SUPPLEMENTAL DATA

ADVANCED ENERGY INDUSTRIES, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS (IN THOUSANDS)

	SEPTEMBER 30, 1996 (UNAUDITED)	DECEMBER 31, 1995
	-----	-----
ASSETS		
Current Assets:		
Cash and cash equivalents.	\$ 8,544	\$13,332
Accounts receivable.	15,813	15,172
Inventories.	15,297	16,104
Prepaid expenses and other current assets.	998	663
Deferred income tax benefit.	1,031	1,031
	-----	-----
Total current assets	41,683	46,302
	-----	-----
Property and Equipment, net.	9,841	6,639
Other Assets	2,596	2,378
	-----	-----
Total assets	\$54,120	\$55,319
	-----	-----
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	\$ 2,607	\$ 6,665
Accrued payroll and employee benefits.	2,510	2,763
Other accrued expenses	755	749
Customer deposits.	125	113
Accrued income tax payable	296	1,336
Current portion of long-term debt.	1,004	927
	-----	-----
Total current liabilities.	7,297	12,553
	-----	-----
Long-term debt	978	1,557
Deferred income tax liability.	122	122
	-----	-----
Total liabilities.	8,397	14,232
	-----	-----
Stockholders' equity	45,723	41,087
	-----	-----
Total liabilities and stockholders' equity	\$54,120	\$55,319
	-----	-----

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

ADVANCED ENERGY INDUSTRIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS
(IN THOUSANDS, EXCEPT PER SHARE AMOUNTS)

QUARTER ENDED SEPTEMBER 30,

	1996 (UNAUDITED)	1995 (UNAUDITED)
Net Sales	\$21,639	\$25,554
Cost of Sales	15,047	12,734
Gross profit	6,592	12,820
Operating Expenses:		
Research and development	3,349	2,711
Sales and marketing	2,201	1,571
General and administrative	933	1,801
Operating Income	109	6,737
Other (expense) income, net	97	(562)
Net income before income taxes	206	6,175
Provision for income taxes	83	2,116
Net Income	\$ 123	\$ 4,059
Net Income per share	\$ 0.01	\$ 0.21
Weighted average shares outstanding	21,622	19,170

NINE MONTHS ENDED SEPTEMBER 30,

	1996 (UNAUDITED)	1995
Net Sales	\$78,636	\$68,538
Cost of Sales	49,286	34,473
Gross profit	29,350	34,065
Operating Expenses:		
Research and development	10,491	7,105
Sales and marketing	6,532	4,293
General and administrative	4,989	5,415
Operating Income	7,338	17,252
Other (expense) income, net	(139)	(466)
Net income before income taxes	7,199	16,786
Provision for income taxes	2,741	6,221
Net Income	\$ 4,458	\$ 10,565
Net Income per share	\$ 0.21	\$ 0.56
Weighted average shares outstanding	21,645	18,887

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

ADVANCED ENERGY INDUSTRIES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS
(IN THOUSANDS)

	NINE MONTHS ENDED SEPTEMBER 30,	
	1996 (UNAUDITED)	1995
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 4,458	\$10,565
Adjustments to reconcile net income to net cash provided by operating activities --		
Depreciation and amortization	1,914	1,170
Deferred income tax benefit	--	(252)
Amortization of deferred compensation	36	--
Loss on disposal of property and equipment	41	--
Changes in operating assets and liabilities --		
Accounts receivable, trade	(520)	(6,859)
Related parties and other receivables	(120)	(983)
Inventories	806	(7,527)
Income taxes	(1,040)	2,390
Other current assets	(335)	(310)
Deposits and other	43	(96)
Demonstration and customer service equipment	(536)	(705)
Accounts payable	(4,058)	4,628
Accrued payroll and employee benefits	(253)	619
Customer deposits and other accrued expenses	18	(108)
Net cash provided by operating activities	454	2,532
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of property and equipment, net	(4,878)	(2,385)
Net cash used in investing activities	(4,878)	(2,385)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from notes payable	--	25,163
Repayment of notes payable and capital lease obligations	(502)	(24,638)
Proceeds from sale of common stock	129	84
Net cash (used in) provided by financing activities	(373)	609
EFFECT OF CUMULATIVE TRANSLATION ADJUSTMENT	9	(399)
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(4,788)	357
CASH AND CASH EQUIVALENTS, beginning of period	13,332	368
CASH AND CASH EQUIVALENTS, end of period	\$ 8,544	\$ 725
SUPPLEMENTAL DISCLOSURE OF NON-CASH INVESTING AND FINANCING ACTIVITIES:		
Deferred compensation on stock options issued	\$ 0	\$ 142
Exercise of stock options in exchange for stockholders' note receivable	\$ 0	\$ 1,083
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid for interest	\$ 143	\$ 469
Cash paid for income taxes	\$ 3,657	\$ 4,083

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

ADVANCED ENERGY INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) BASIS OF PRESENTATION AND MANAGEMENT OPINION

In the opinion of management, the accompanying unaudited consolidated balance sheets and statements of operations and cash flows contain all adjustments, consisting only of normal recurring items, necessary to present fairly the financial position of Advanced Energy Industries, Inc., a Delaware corporation, and its wholly owned subsidiaries (the "Company") at September 30, 1996, its results of operations and cash flows for the three and nine month periods ended September 30, 1996 and September 30, 1995.

The unaudited financial statements presented herein have been prepared in accordance with the instructions to Form 10-Q and do not include all the information and note disclosures required by generally accepted accounting principles. The financial statements should be read in conjunction with the audited financial statements and notes thereto contained in the Company's latest annual report on Form 10-K for the year ended December 31, 1995.

(2) INITIAL PUBLIC OFFERING

In November 1995, the Company closed on the initial public offering of its common stock. In connection with the offering, 2,400,000 shares of previously unissued common shares were sold at a price of \$10 per share, providing gross proceeds of \$24,000,000, less \$2,790,000 in offering costs.

(3) ACCOUNTS RECEIVABLE

Accounts receivable consisted of the following:

	SEPTEMBER 30, 1996 (UNAUDITED)	DECEMBER 31, 1995
	(IN THOUSANDS)	
Domestic	\$ 9,350	\$ 8,825
Foreign.	4,916	4,925
Allowance for doubtful accounts.	(206)	(210)
	-----	-----
Trade accounts receivable.	\$14,060	\$13,540
Related parties.	909	979
Other.	844	653
	-----	-----
Total accounts receivable.	\$15,813	\$15,172
	-----	-----

(4) INVENTORIES

Inventories consisted of the following:

	SEPTEMBER 30, 1996 (UNAUDITED)	DECEMBER 31, 1995
	(IN THOUSANDS)	
Parts and raw materials.	\$11,060	\$11,104
Work in process.	1,672	1,936
Finished goods	2,565	3,064
	-----	-----
	\$15,297	\$16,104
	-----	-----

(5) NET INCOME PER COMMON SHARE

Net income per share is computed based on results of operations attributable to common stock and weighted average number of common and common equivalent shares outstanding during each of the periods. Earnings per share are calculated by dividing the net earnings by the weighted average of common and common equivalent shares outstanding during each of the periods.

(6) STOCKHOLDERS' EQUITY

Stockholders' equity consisted of the following:

SEPTEMBER 30,	DECEMBER 31,
1996	1995
(UNAUDITED)	
-----	-----

(IN THOUSANDS,
EXCEPT PAR VALUE)

Common stock, \$0.001 par value, 30,000 shares authorized; 21,251 and 21,069 shares issued

and outstanding.	\$ 21	\$ 21
Additional paid-in capital	23,057	22,925
Retained earnings.	24,380	19,921
Stockholders' notes receivable	(1,083)	(1,083)
Deferred compensation.	(94)	(130)
Cumulative translation adjustment.	(558)	(567)
	-----	-----
Total stockholders' equity	\$45,723	\$41,087
	-----	-----

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

The following discussion contains, in addition to historical information, forward-looking statements. The Company's actual results may differ significantly from the results discussed in the forward-looking statements. Factors that could cause or contribute to such differences include, but are not limited to, those discussed below and in the Company's 1995 annual report on Form 10-K.

In particular, the Company believes that the following factors could impact forward-looking statements made herein or in future written or oral releases and by hindsight, prove such statements to be overly optimistic and unachievable: volatility of the semiconductor and semiconductor equipment industries, customer concentration, dependence on design wins, rapid technological change and dependence on new system introduction, competition, and management of growth.

RESULTS OF OPERATIONS FOR THE THREE MONTHS ENDED SEPTEMBER 30, 1996 AND 1995

SALES

Sales for the third quarter of 1996 were \$21.6 million, a decrease of 16% from third quarter of 1995 sales of \$25.6 million. The Company's sales decline in the third quarter of 1996 resulted from the decreased unit sales of the Company's systems and a change in product mix, which also reduced the average selling price for the period. A significant part of this unit sales decrease is attributable to decreased demand by domestic semiconductor equipment customers, primarily the Company's two largest customers.

The Company continues to be cautious about the outlook for future sales to the semiconductor equipment industry. During the most recent quarter, 52% of the Company's revenue came from this industry, down from 57% in the same quarter a year ago.

GROSS MARGIN

The Company's gross margin for the third quarter of 1996 was 30.5% of revenue, down from 50.2% of revenue in the comparable period in 1995, and down from 42.3% in the second quarter of 1996. The decline in gross margin in the third quarter of 1996 was primarily the result of underabsorbed fixed manufacturing costs. Revenues in the current quarter were \$3.9 million lower than in the third quarter of 1995 and \$8.2 million lower than in the second quarter of 1996, while fixed overhead expenses were increased during 1995 and early 1996 to provide higher capacity. The Company expects underabsorption of manufacturing overhead will continue to adversely impact gross margin until sales

levels improve. Additionally, gross margin was negatively impacted by a shift in product mix toward products on which material costs increased as a percentage of sales and by increased customer service costs, which increased as a percentage of sales, as a result of the lower sales base.

During the third quarter, the Company announced cost containment measures in response to recent declines in orders to the semiconductor capital equipment market. As part of these measures, the Company reduced headcount by 7 percent, reduced leased facilities by 7 percent, initiated a 10% decrease in senior management salaries and reevaluated inventories for excess and obsolete parts. These efforts resulted in additional charges of \$350K related to severance pay, charges associated with subleasing facilities and an increased provision for excess inventories.

RESEARCH AND DEVELOPMENT

The Company's research and development costs are associated with researching new technologies, developing new products and improving existing product designs. Research and development expenses for the third quarter of 1996 were \$3.3 million, compared to expenses of \$2.7 million in the third quarter of 1995, representing an increase of 22%. As a percentage of sales, research and development expenses increased to 15.5% in the third quarter of 1996 from 10.6% in the third quarter of 1995. The increase is primarily associated with costs incurred to support new product development.

The Company believes that continued research and development investment is essential to ongoing development of new products. Since inception, all research and development costs have been internally funded and expensed.

SALES AND MARKETING

Sales and marketing expenses support domestic and international sales and marketing activities which include personnel, trade shows, advertising, and other marketing activities. Sales and marketing expenses for the third quarter of 1996 were \$2.2 million, compared to expenses of \$1.6 million in the third quarter of 1995, representing an increase of 38%. As a percentage of sales, sales and marketing expenses increased to 10.2% in the third quarter of 1996 from 6.1% in the third quarter of 1995. The dollar increase is attributable to costs associated with expansion of the sales and marketing infrastructure to support the sales volume increase realized in the second quarter of 1996. As a percentage of sales, the major increase is a result of the lower sales base.

The Company is reorganizing its sales and marketing team to better address the specific needs of its customers. As a result, sales and marketing expenses are expected to increase as a percentage of sales in future periods.

GENERAL AND ADMINISTRATIVE

General and administrative expenses support the worldwide financial, administrative, information systems and human resources functions of the Company. General and administrative expenses for the third quarter of 1996 were \$0.9 million, compared to expenses of \$1.8 million in the third quarter of 1995, representing a decrease of 42%. As a percentage of sales, these expenses decreased to 4.3% in the third quarter of 1996 from 7.0% in the third quarter of 1995. The decrease during the third quarter was primarily attributed to reductions made to previously accrued bonuses and other employee benefits.

The Company is currently implementing information management system software which will replace existing systems to support its growth. The Company expects that significant charges related to training and implementation of the new software will occur during 1996 and 1997. The expenses incurred to date have been recognized in the appropriate functional area.

OTHER INCOME (EXPENSE)

Other income and expense consists primarily of foreign exchange gains and losses, interest expense and other miscellaneous income and expense items. Other income was \$0.1 million for the third quarter of 1996, compared to other expenses of \$0.6 million in the third quarter of 1995.

The Company has experienced fluctuations in foreign currency exchange rates during the past few months. As a hedge against significant currency fluctuations in the Japanese yen, the Company has entered into various forward foreign exchange contracts to lessen exposures to foreign exchange losses.

PROVISION FOR INCOME TAXES

The income tax provision of \$0.1 million for the third quarter of 1996 represented an estimated effective rate of 40.3%. The income tax provision in the comparable period in 1995 was \$2.1 million, representing an estimated rate of 34.3%. The Company adjusts its income taxes periodically based upon the anticipated tax status of all foreign and domestic entities.

RESULTS OF OPERATIONS FOR THE NINE MONTHS ENDED SEPTEMBER 30, 1996 AND 1995

SALES

Sales for the first nine months of 1996 were \$78.6 million, an increase of 15% from sales of \$68.5 million in the comparable period in 1995. The Company's sales growth during the periods presented has resulted from the increased unit sales of the Company's

systems, primarily in the first half of 1996. A significant part of this growth is attributable to higher sales to domestic customers, primarily the Company's two largest customers.

GROSS MARGIN

The Company's gross margin for the first nine months of 1996 was 37.3% of revenue, down from 49.7% of revenue in the comparable period in 1995. The decline in gross margin in the first nine months of 1996 was primarily affected by higher material costs associated with outsourcing assemblies, changes in product mix, including some shift toward lower margin CE products, and underabsorbed overhead costs. Average selling prices for the two comparative nine month periods remained relatively constant.

RESEARCH AND DEVELOPMENT

Research and development expenses for the first nine months of 1996 were \$10.5 million, compared to expenses of \$7.1 million in the comparable period in 1995, representing an increase of 48%. As a percentage of sales, research and development expenses increased to 13.3% in the first nine months of 1996 from 10.4% in the first nine months of 1995. The increase is primarily associated with costs incurred to support new product development.

SALES AND MARKETING

Sales and marketing expenses for the first nine months of 1996 were \$6.5 million, compared to expenses of \$4.3 million in the comparable period in 1995, representing an increase of 51%. As a percentage of sales, these expenses increased to 8.3% in the first nine months of 1996 from 6.3% in the first nine months of 1995. The increase is attributable to costs associated with expansion to support the increase in sales volume, and to provide additional support to customers.

GENERAL AND ADMINISTRATIVE

General and administrative expenses for the first nine months of 1996 were \$5.0 million, compared to expenses of \$5.4 million in the comparable period in 1995, representing a decrease of 7%. As a percentage of sales, these expenses decreased to 6.3% in the first nine months of 1996 from 7.9% in the first nine months of 1995. The decrease in general and administrative expenses as a percentage of sales was primarily attributed to reductions made to previously accrued bonuses and other employee benefits.

OTHER INCOME (EXPENSE)

Other expenses were \$0.1 million for the first nine months of 1996, compared to \$0.5 million in the comparable period in 1995.

PROVISION FOR INCOME TAXES

The income tax provision of \$2.7 million for the first nine months of 1996 represented an estimated effective rate of 38.1%. The income tax provision in the comparable period in 1995 was \$6.2 million, representing an estimated rate of 37.1%. The Company periodically adjusts its income tax provision based upon the anticipated tax status of all foreign and domestic entities.

LIQUIDITY AND CAPITAL RESOURCES

Until the initial public offering of the Company's common stock in November 1995, the Company financed its operations, acquired equipment and met its working capital requirements through borrowings under its revolving line of credit, long-term loans secured by property and equipment and cash flow from operations.

Cash provided by operations totaled \$0.5 million for the first nine months in 1996 compared to \$2.5 million for the same period in 1995. Cash provided in the first nine months of 1996 was primarily a result of net income offset by decreases in accounts payable. Cash provided in the comparable period in 1995 was primarily a result of net income and increases in accounts payable and income taxes payable offset by increases in accounts receivable and inventories.

Investing activities, consisting primarily of equipment acquisitions and leasehold improvements, used cash of \$4.9 million in the first nine months of 1996, versus \$2.4 million in the comparable period in 1995. Financing activities in the first nine months of 1996 consisted primarily of note and loan repayments and used cash of \$0.4 million. In the comparable period in 1995, financing activities consisted primarily of proceeds from and repayments to the Company's revolving line of credit, proceeds from notes payable, and repayment of notes payable and capital lease obligations and generated cash of \$0.6 million.

The Company plans to spend approximately \$0.4 million through the remainder of 1996 for the acquisition of equipment and integrated information management system software, leasehold improvements and furnishings.

As of September 30, 1996, the Company had working capital of \$34.4 million. The Company's principal sources of liquidity consisted of \$8.5 million of cash and cash equivalents and \$8.0 million available under an \$8.0 million revolving line of credit that bears interest at the prime rate (8.25% at October 15, 1996). The Company has the option to convert up to \$3.0 million of its revolving line of credit to a 36-month term loan that would bear interest at prime rate plus 0.50%.

The Company also has a term loan for equipment financing for its US operations. At September 30, 1996, \$1.2 million was outstanding under the term loan, which bears

interest at prime plus 0.75% and is due July 31, 1999. During the third quarter, the Company entered into an agreement for a term loan of \$0.2 million to provide working capital for its Japan operations. The Company also entered into an agreement in November 1995, that provides the Company with a \$1.5 million line of credit to purchase equipment. At September 30, 1996, there were no amounts outstanding under this line of credit.

The Company believes that its cash and cash equivalents, cash flow from operations and available borrowings, will be sufficient to meet the Company's working capital needs through at least the first half of 1997. After that time, the Company may require additional equity or debt financing to address its working capital, capital equipment, or expansion needs. There can be no assurance that additional funding will be available when required or that it will be available on terms acceptable to the Company.

PART II OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

None.

ITEM 2. CHANGES IN SECURITIES

None.

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

None.

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, thereunto duly authorized.

ADVANCED ENERGY INDUSTRIES, INC.

November 12, 1996

/s/ RICHARD P. BECK

(Registrant)
Vice President, Chief Financial
Officer, Assistant Secretary and
Director (Principal Financial Officer
and Principal Accounting Officer)

ARTICLE 5

PERIOD TYPE	9 MOS
FISCAL YEAR END	DEC 31 1996
PERIOD END	SEP 30 1996
CASH	8,544
SECURITIES	0
RECEIVABLES	15,813
ALLOWANCES	0
INVENTORY	15,297
CURRENT ASSETS	41,683
PP&E	9,841
DEPRECIATION	0
TOTAL ASSETS	54,120
CURRENT LIABILITIES	7,297
BONDS	0
PREFERRED MANDATORY	0
PREFERRED	0
COMMON	21
OTHER SE	45,702
TOTAL LIABILITY AND EQUITY	54,120
SALES	78,636
TOTAL REVENUES	78,636
CGS	49,286
TOTAL COSTS	49,286
OTHER EXPENSES	22,012
LOSS PROVISION	0
INTEREST EXPENSE	143
INCOME PRETAX	7,199
INCOME TAX	2,741
INCOME CONTINUING	4,458
DISCONTINUED	0
EXTRAORDINARY	0
CHANGES	0
NET INCOME	4,458
EPS PRIMARY	0.21
EPS DILUTED	0.21

End of Filing

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