

HURCO COMPANIES INC
Form 10-Q
March 08, 2007

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 January 31, 2007 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 No. 0-9143

HURCO COMPANIES, INC.

(Exact name of registrant as specified in its charter)

Indiana

(State or other jurisdiction of
incorporation or organization)

35-1150732

(I.R.S. Employer Identification Number)

**One Technology Way
Indianapolis, Indiana**

(Address of principal executive offices)

46268

(Zip code)

Registrant's telephone number, including area code **(317) 293-5309**

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Sections 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months, and (2) has been subject to the filing requirements for the past 90 days:

Yes No

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. (Check one):

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 []

The number of shares of the Registrant's common stock outstanding as of March 7, 2007 was 6,389,720.

HURCO COMPANIES, INC.
January 2007 Form 10-Q Quarterly Report

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PART I - FINANCIAL INFORMATION**Item 1. FINANCIAL STATEMENTS****HURCO COMPANIES, INC.
CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS**

(In thousands, except per share data)

| | Three Months Ended January 31 | |
|---|--|-----------------|
| | 2007 | 2006 |
| | (unaudited) | |
| Sales and service fees | \$ 46,878 | \$ 31,894 |
| Cost of sales and service | 29,554 | 20,967 |
| Gross profit | 17,324 | 10,927 |
| Selling, general and administrative expenses | 9,250 | 6,296 |
| Operating income | 8,074 | 4,631 |
| Interest expense | 43 | 84 |
| Other expense (income), net | (362) | (104) |
| Income before taxes | 8,393 | 4,651 |
| Provision for income taxes | 2,998 | 1,618 |
| Net income | \$ 5,395 | \$ 3,033 |
| Earnings per common share | | |
| Basic | \$ 0.85 | \$ 0.49 |
| Diluted | \$ 0.84 | \$ 0.48 |
| Weighted average common shares outstanding | | |
| Basic | 6,362 | 6,242 |
| Diluted | 6,418 | 6,328 |

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

HURCO COMPANIES, INC.
CONDENSED CONSOLIDATED BALANCE SHEET
(Dollars in thousands)

| | January 31 2007 (unaudited) | October 31 2006 (audited) |
|---|--|--|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 32,326 | \$ 29,846 |
| Accounts receivable | 25,169 | 22,248 |
| Inventories | 40,324 | 43,343 |
| Deferred tax assets | 1,910 | 2,768 |
| Other | 3,170 | 2,677 |
| Total current assets | 102,899 | 100,882 |
| Property and equipment: | | |
| Land | 761 | 761 |
| Building | 7,234 | 7,234 |
| Machinery and equipment | 13,230 | 12,952 |
| Leasehold improvements | 1,167 | 1,147 |
| | 22,932 | 22,094 |
| Less accumulated depreciation and amortization | (13,262) | (12,944) |
| | 9,130 | 9,150 |
| Non-current assets: | | |
| Deferred tax assets | 1,088 | 1,121 |
| Software development costs, less accumulated amortization | 5,894 | 5,580 |
| Investments and other assets | 7,812 | 7,381 |
| | \$ 126,823 | \$ 124,114 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 24,227 | \$ 26,605 |
| Accrued expenses | 16,338 | 17,599 |
| Current portion of long-term debt | 138 | 136 |
| Total current liabilities | 40,703 | 44,340 |
| Non-current liabilities: | | |
| Long-term debt | 3,839 | 3,874 |
| Deferred credits and other | 588 | 525 |
| Total liabilities | 45,130 | 48,739 |
| Shareholders' equity: | | |
| Preferred stock: no par value per share; 1,000,000 shares authorized; no shares issued | | |
| Common stock: no par value; \$.10 stated value per share; 12,500,000 shares authorized, and 6,380,520 and 6,346,520 shares issued and outstanding, respectively | 638 | 635 |
| Additional paid-in capital | 50,528 | 50,011 |
| Retained earnings | 33,875 | 28,480 |

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| | | |
|--|------------|------------|
| Accumulated other comprehensive income | (3,348) | (3,751) |
| Total shareholders' equity | 81,693 | 75,375 |
| | \$ 126,823 | \$ 124,114 |

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

HURCO COMPANIES, INC.
CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS
(Dollars in thousands)

| | Three Months Ended | |
|---|---------------------------|------------------|
| | January 31 | |
| | 2007 | 2006 |
| | (unaudited) | |
| Cash flows from operating activities: | | |
| Net income | \$ 5,395 | \$ 3,033 |
| Adjustments to reconcile net income to Net cash provided by (used for) operating activities: | | |
| Provision for doubtful accounts | (38) | 16 |
| Equity in (income) loss of affiliates | (204) | (96) |
| Depreciation and amortization | 388 | 365 |
| Stock-based compensation | 308 | 5 |
| Change in assets and liabilities: | | |
| (Increase) decrease in accounts receivable | (2,587) | 1,606 |
| (Increase) decrease in inventories | 3,695 | (979) |
| Increase (decrease) in accounts payable | (2,634) | 1,967 |
| Increase (decrease) in accrued expenses | (1,797) | (2,559) |
| Increase (decrease) in deferred taxes | 77 | 410 |
| Other | 306 | (313) |
| Net cash provided by operating activities | 2,909 | 3,455 |
| Cash flows from investing activities: | | |
| Purchase of property and equipment | (149) | (60) |
| Software development costs | (505) | (432) |
| Other investments | (299) | (159) |
| Net cash used for investing activities | (953) | (651) |
| Cash flows from financing activities: | | |
| Repayment on first mortgage | (33) | (30) |
| Tax benefit from exercise of stock options | 115 | 499 |
| Proceeds from exercise of common stock options | 97 | 530 |
| Net cash provided by financing activities | 179 | 999 |
| Effect of exchange rate changes on cash | 345 | 200 |
| Net increase in cash and cash equivalents | 2,480 | 4,003 |
| Cash and cash equivalents at beginning of period | 29,846 | 17,559 |
| Cash and cash equivalents at end of period | \$ 32,326 | \$ 21,562 |

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

HURCO COMPANIES, INC.
CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY
For the three months ended January 31, 2007 and 2006

| (Dollars in thousands except Shares Issued and Outstanding) | Common Stock | | Additional | Retained | Accumulated Other Comprehensive | | |
|--|-----------------------------------|---------------|--|-----------------------|---------------------------------------|--|------------------|
| | Shares Issued & Outstanding | Amount | Paid-In Capital (Dollars in thousands) | Earnings (Deficit) | Income (Loss) | | Total |
| Balances, October 31, 2005 | 6,220,220 | \$ 622 | \$ 48,701 | \$ 13,001 | \$ (3,380) | | \$ 58,944 |
| Net income | -- | -- | -- | 3,033 | -- | | 3,033 |
| Translation of foreign currency financial statements | -- | -- | -- | -- | 556 | | 556 |
| Unrealized gain on derivative instruments | -- | -- | -- | -- | 584 | | 584 |
| Comprehensive income | -- | -- | -- | -- | -- | | 4,173 |
| Exercise of common stock options | 120,800 | 12 | 518 | -- | -- | | 530 |
| Tax benefit from exercise of stock options | -- | -- | 499 | -- | -- | | 499 |
| Stock-based compensation expense | -- | -- | 5 | -- | -- | | 5 |
| Balances, January 31, 2006 | 6,341,020 | \$ 634 | \$ 49,723 | \$ 16,034 | \$ (2,240) | | \$ 64,151 |
| Balances, October 31, 2006 | 6,346,520 | \$ 635 | \$ 50,011 | \$ 28,480 | \$ (3,751) | | \$ 75,375 |
| Net income | -- | -- | -- | 5,395 | -- | | 5,395 |
| Translation of foreign currency financial statements | -- | -- | -- | -- | 638 | | 638 |

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| | | | | | | |
|--|------------------|---------------|------------------|------------------|-------------------|------------------|
| Unrealized loss on derivative instruments | -- | -- | -- | -- | (235) | (235) |
| Comprehensive income | -- | -- | -- | -- | -- | 5,798 |
| Exercise of common stock options | 34,000 | 3 | 94 | -- | -- | 97 |
| Tax benefit from exercise of stock options | -- | -- | 115 | -- | -- | 115 |
| Stock-based compensation expense | -- | -- | 308 | -- | -- | 308 |
| Balances, January 31, 2007 | 6,380,520 | \$ 638 | \$ 50,528 | \$ 33,875 | \$ (3,348) | \$ 81,693 |

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

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. GENERAL

The unaudited Condensed Consolidated Financial Statements include the accounts of Hurco Companies, Inc. and its consolidated subsidiaries. As used in this report, and unless the context indicates otherwise, the terms “we”, “us”, “our” and similar language refer to Hurco Companies, Inc. and its consolidated subsidiaries. We design and produce computerized machine tools, interactive computer control systems and software for sale through our distribution network to the worldwide metal cutting market. We also provide software options, computer control upgrades, accessories and replacement parts for our products, as well as customer service and training support.

The condensed financial information as of January 31, 2007 and for the three months ended January 31, 2007 and January 31, 2006 is unaudited; however, in our opinion, the interim data include all adjustments, consisting only of normal recurring adjustments, necessary for a fair statement of our results for, and our financial position at the end of the interim periods. We suggest that you read these condensed consolidated financial statements in conjunction with the financial statements and the notes thereto included in our Annual Report on Form 10-K for the year ended October 31, 2006.

2. HEDGING

We enter into foreign currency forward exchange contracts periodically to hedge certain forecast inter-company sales and forecast inter-company and third party purchases denominated in foreign currencies (the Pound Sterling, Euro and New Taiwan Dollar). The purpose of these instruments is to mitigate the risk that the U.S. Dollar net cash inflows and outflows resulting from sales and purchases denominated in foreign currencies will be adversely affected by changes in exchange rates. These forward contracts have been designated as cash flow hedge instruments, and are recorded in the Condensed Consolidated Balance Sheets at fair value in Other Current Assets and Accrued Expenses. Gains and losses resulting from changes in the fair value of these hedge contracts are deferred in Accumulated Other Comprehensive Income and recognized as an adjustment to Cost of Sales in the period that the sale that is the subject of the related hedge contract is recognized, thereby providing an offsetting economic impact against the corresponding change in the U.S. Dollar value of the inter-company sale or purchase being hedged.

At January 31, 2007, we had \$684,000 of losses related to cash flow hedges deferred in Accumulated Other Comprehensive Income, net of tax. Of this amount, \$519,000 represented unrealized losses related to future cash flow hedge instruments that remain subject to currency fluctuation risk. These deferred losses will be recorded as an adjustment to Cost of Sales in the periods through December 2007, in which the sale that is the subject of the related hedge contract is recognized, as described above. Net losses on cash flow hedge contracts, which we reclassified from Other Comprehensive Income to Cost of Sales in the quarter ended January 31, 2007, were \$262,000 compared to net gains of \$182,000 for the same period in the prior year.

We also enter into foreign currency forward exchange contracts to protect against the effects of foreign currency fluctuations on receivables and payables denominated in foreign currencies. These derivative instruments are not designated as hedges under Statement of Financial Accounting Standards No. 133, “Accounting Standards for Derivative Instruments and Hedging Activities” (SFAS 133), and, as a result, changes in their fair value are reported currently as Other Expense (Income), Net in the Consolidated Statement of Operations consistent with the transaction gain or loss on the related foreign denominated receivable or payable. We recorded net transaction gains of \$16,000 for the quarter ended January 31, 2007 compared to net losses of \$40,000 for the same period in the prior year.

3. STOCK OPTIONS

We have a stock option plan that allows us to grant awards of options to purchase shares of our common stock, stock appreciation rights, restricted shares and performance shares. Options granted under the plan are exercisable for a period up to ten years after the date of grant and vest in equal annual installments as specified by the Compensation Committee of our Board of Directors at the time of grant. The exercise price of options intended to qualify as incentive stock options may not be less than 100% of the fair market value of a share of common stock on the date of grant. During the first three months of fiscal 2007, options to purchase 34,000 shares were exercised, resulting in cash proceeds of approximately \$97,000 and an additional tax benefit of approximately \$115,000, compared to 120,800 shares exercised in the prior year period resulting in cash proceeds of \$530,000 and an additional tax benefit of approximately \$499,000.

Effective November 1, 2005, we adopted SFAS No. 123(R), "Share Based Payment," using the modified prospective method, and began applying its provisions to all options granted as well as to the nonvested portion of previously granted options outstanding at that date. Compensation expense is determined at the date of grant using the Black-Scholes valuation model.

On November 16, 2006, the Compensation Committee of the Board of Directors granted 40,000 shares under the 1997 Plan to certain employees and directors. The fair value of options awarded was estimated on the date of grant using a Black-Scholes valuation model with assumptions for expected volatility based on the historical volatility of the Company's stock, contractual term of the options of ten years and a risk-free interest rate based upon a three-year U.S. Treasury yield as of the date of grant. The options granted to employees vest in three equal annual installments and the directors' options were granted with immediate vesting as of the date of grant.

The weighted-average fair value of options granted during the quarter ended January 31, 2007 was \$22.84 and \$24.97 for employees and directors, respectively. During the quarter ended January 31, 2007 approximately \$308,000 of stock-based compensation expense had been recorded related to options granted under the 1997 Plan compared to \$5,000 for the same period in the prior year. As of January 31, 2007 there was approximately \$628,000 of total unrecognized stock-based compensation cost that is expected to be recognized over the next three years.

A summary of stock option activity for the three-month period ended January 31, 2007, is as follows:

| | Stock Options | Weighted Average Exercise Price |
|---------------------------------|---------------|---------------------------------------|
| Outstanding at October 31, 2006 | 88,700 | \$ 2.46 |
| Options granted | 40,000 | \$ 26.69 |
| Options exercised | (34,000) | \$ 2.86 |
| Options cancelled | - | - |
| Outstanding at January 31, 2007 | 94,700 | \$ 12.55 |

The total intrinsic value of stock options exercised during the three-month periods ended January 31, 2007 and 2006 was approximately \$1.0 million and \$3.6 million, respectively. The intrinsic value is calculated as the difference between the stock price as of January 31, 2007 and the exercise price of the stock option multiplied by the number of shares exercised.

Summarized information about outstanding stock options as of January 31, 2007, that are already vested and those that we expect to vest, as well as stock options that are currently exercisable, is as follows:

| | Outstanding Stock Options Already Vested and Expected to Vest | Options that are outstanding and Exercisable |
|-------------------------------|--|--|
| Number of outstanding options | | |