

ADVANCED ENERGY INDUSTRIES INC

Form 10-Q

May 08, 2012

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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended March 31, 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: 000-26966

ADVANCED ENERGY INDUSTRIES, INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

1625 Sharp Point Drive, Fort Collins, CO

(Address of principal executive offices)

84-0846841

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

80525

(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 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 (§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 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. (Check one):

Large accelerated filer Accelerated filer 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

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As of April 30, 2012, there were 39,731,792 shares of the registrant's Common Stock, par value \$0.001 per share, outstanding.

ADVANCED ENERGY INDUSTRIES, INC.
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PART I FINANCIAL STATEMENTS

ITEM 1. UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

ADVANCED ENERGY INDUSTRIES, INC.

Condensed Consolidated Balance Sheets *

(In thousands, except per share amounts)

	March 31, 2012	December 31, 2011
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 125,418	\$ 117,639
Marketable securities	25,325	25,567
Accounts receivable, net of allowances of \$6,693 and \$6,796, respectively	103,414	132,485
Inventories, net of reserves of \$14,711 and \$13,614, respectively	83,164	80,283
Deferred income tax assets	9,011	9,014
Income taxes receivable	14,863	13,826
Other current assets	10,730	11,672
Total current assets	371,925	390,486
Property and equipment, net	41,247	42,338
OTHER ASSETS:		
Deposits and other	9,031	8,959
Goodwill	46,515	46,515
Other intangible assets, net	42,066	43,438
Deferred income tax assets	1,706	1,642
Total assets	\$512,490	\$533,378
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	\$38,225	\$44,828
Income taxes payable	2,670	3,310
Accrued payroll and employee benefits	9,565	9,184
Accrued warranty expense	8,747	8,433
Other accrued expenses	11,227	10,800
Customer deposits	8,180	14,689
Total current liabilities	78,614	91,244
LONG-TERM LIABILITIES:		
Deferred income tax liabilities	6,999	6,475
Uncertain tax positions	16,404	16,404
Accrued warranty expense	5,572	6,286
Other long-term liabilities	15,349	5,630
Total liabilities	122,938	126,039
Commitments and contingencies (Note 16)		
STOCKHOLDERS' EQUITY:		
Preferred stock, \$0.001 par value, 1,000 shares authorized, none issued and outstanding		
Common stock, \$0.001 par value, 70,000 shares authorized; 40,056 and 41,956 issued and outstanding, respectively	40	42
Additional paid-in capital	236,928	254,003
Retained earnings	125,836	124,767
Accumulated other comprehensive income	26,748	28,527
Total stockholders' equity	389,552	407,339
Total liabilities and stockholders' equity	\$512,490	\$533,378

* Amounts as of March 31, 2012 are unaudited. Amounts as of December 31, 2011 are derived from the December 31, 2011 audited Consolidated Financial Statements.

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

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ADVANCED ENERGY INDUSTRIES, INC.
Condensed Consolidated Statements of Operations (Unaudited)
(In thousands, except per share amounts)

	Three Months Ended March 31,	
	2012	2011
SALES	\$ 105,787	\$ 137,652
COST OF SALES	66,043	75,607
GROSS PROFIT	39,744	62,045
OPERATING EXPENSES:		
Research and development	15,115	15,862
Selling, general, and administrative	20,059	20,905
Amortization of intangible assets	1,372	921
Restructuring charges	2,575	—
Total operating expenses	39,121	37,688
OPERATING INCOME	623	24,357
OTHER INCOME, NET	411	663
Income from continuing operations before income taxes	1,034	25,020
Provision for income taxes	268	6,254
INCOME FROM CONTINUING OPERATIONS, NET OF INCOME TAXES	766	18,766
Income from discontinued operations, net of income taxes	303	140
NET INCOME	\$ 1,069	\$ 18,906
Basic weighted-average common shares outstanding	40,781	43,440
Diluted weighted-average common shares outstanding	41,292	44,133
EARNINGS PER SHARE:		
CONTINUING OPERATIONS:		
BASIC EARNINGS PER SHARE	\$0.02	\$0.43
DILUTED EARNINGS PER SHARE	\$0.02	\$0.43
DISCONTINUED OPERATIONS		
BASIC EARNINGS PER SHARE	\$0.01	\$0.00
DILUTED EARNINGS PER SHARE	\$0.01	\$0.00
NET INCOME:		
BASIC EARNINGS PER SHARE	\$0.03	\$0.44
DILUTED EARNINGS PER SHARE	\$0.03	\$0.43

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

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ADVANCED ENERGY INDUSTRIES, INC.
 Condensed Consolidated Statements of Comprehensive Income (Unaudited)
 (In thousands)

	Three months ended March	
	31,	
	2012	2011
Net income	1,069	18,906
Other comprehensive income, net of tax:		
Foreign currency translation adjustment	(1,798	) (287
Unrealized gains (losses) on securities	19	(3
Comprehensive income (loss)	(710	) 18,616

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

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ADVANCED ENERGY INDUSTRIES, INC.
Condensed Consolidated Statements of Cash Flows (Unaudited)
(In thousands)

	Three Months Ended March 31,	
	2012	2011
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$1,069	\$18,906
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	4,213	3,263
Stock-based compensation expense	5,009	2,740
Provision (benefit) for deferred income taxes	478	(180)
Restructuring charges	2,575	—
Net loss on disposal of assets	632	556
Changes in operating assets and liabilities:		
Accounts receivable	28,760	(904)
Inventories	(2,306)	(11,927)
Other current assets	1,108	3,490
Accounts payable	(6,824)	(4,212)
Other current liabilities and accrued expenses	1,753	(9,751)
Income taxes	(1,776)	386
Non-current liabilities	—	348
Net cash provided by operating activities	34,691	2,715
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of marketable securities	(4,335)	) 22
Proceeds from sale of marketable securities	4,563	2,000
Proceeds from the sale of assets	—	16
Purchases of property and equipment	(3,120)	) (4,428)
Net cash used in investing activities	(2,892)	) (2,390)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Payments on capital lease obligations	(23)	) (39)
Purchase and retirement of treasury stock	(21,934)) —
Proceeds from exercise of stock options	101	1,621
Excess tax from stock-based compensation deduction	(254)	) (88)
Net cash provided by (used in) financing activities	(22,110)	) 1,494
EFFECT OF CURRENCY TRANSLATION ON CASH	(1,910)	) (315)
INCREASE IN CASH AND CASH EQUIVALENTS	7,779	1,504
CASH AND CASH EQUIVALENTS, beginning of period	117,639	130,914
CASH AND CASH EQUIVALENTS, end of period	\$125,418	\$132,418
SUPPLEMENTAL DISCLOSURE OF CASH FLOW INFORMATION:		
Cash paid for interest	\$14	\$10
Cash paid for income taxes	1,168	6,246
Cash received for refunds of income taxes	5	176
Cash held in banks outside the United States	57,034	58,494

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

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ADVANCED ENERGY INDUSTRIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1. BASIS OF PRESENTATION

We design, manufacture, sell, and support power conversion products that transform power into various usable forms. Our products enable manufacturing processes that use thin-film deposition for various products, such as semiconductor devices, flat panel displays, solar panels, and architectural glass. We also supply thermal instrumentation products for advanced temperature control in the thin-film process for these same markets. Our solar inverter products support renewable power generation solutions for residential, commercial, and utility-scale solar projects and installations. Our network of global service support centers offer repair services, conversions, upgrades, and refurbishments to companies using our products. We also offer a wide variety of operations and maintenance service plans that can be tailored for individual photovoltaic ("PV") sites of all sizes.

We are organized into two strategic business units ("SBU") based on the products and services provided.

Thin Films Processing Power Conversion and Thermal Instrumentation ("Thin Films") SBU offers our products for direct current ("DC"), pulsed DC mid frequency, and radio frequency ("RF") power supplies, matching networks and RF instrumentation as well as thermal instrumentation products.

Solar Energy SBU offers both a transformer-based or transformerless advanced grid-tied PV inverter solution for residential, commercial and utility-scale system installations. Our PV inverters are designed to convert renewable solar power, drawn from large and small scale solar arrays, into high-quality, reliable electrical power.

In the opinion of management, the accompanying unaudited Condensed Consolidated Financial Statements contain all adjustments, consisting of normal, recurring adjustments, necessary to present fairly the financial position of Advanced Energy Industries, Inc., a Delaware corporation, and its wholly-owned subsidiaries ("we", "us", "our", "Advanced Energy", or the "Company") at March 31, 2012, and the results of our operations and cash flows for the three months ended March 31, 2012 and 2011.

The Condensed Consolidated Financial Statements included herein have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission ("SEC"). Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America ("U.S. GAAP") have been condensed or omitted pursuant to such rules and regulations. These unaudited Condensed Consolidated Financial Statements should be read in conjunction with the audited Consolidated Financial Statements and Notes thereto contained in our Annual Report on Form 10-K for the fiscal year ended December 31, 2011 and other financial information filed with the SEC.

ESTIMATES AND ASSUMPTIONS

The preparation of our Condensed Consolidated Financial Statements in conformity with U.S. GAAP requires us to make estimates, assumptions and judgments 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 revenue and expenses during the reporting period. We believe that the significant estimates, assumptions, and judgments when accounting for items and matters such as allowances for doubtful accounts, excess and obsolete inventory, warranty reserves, acquisitions, asset valuations, goodwill, asset life, depreciation, amortization, recoverability of assets, impairments, deferred revenue, stock option and restricted stock grants, taxes, and other provisions are reasonable, based upon information available at the time they are made. Actual results may differ from these estimates, making it possible that a change in these estimates could occur in the near term.

REVENUE RECOGNITION

Our accounting policies are described in our audited Consolidated Financial Statements and Notes thereto contained in our Annual Report on Form 10-K for the year ended December 31, 2011.

NEW ACCOUNTING STANDARDS

From time to time, the Financial Accounting Standards Board ("FASB") or other standards setting bodies issue new accounting pronouncements. Updates to the FASB Accounting Standards Codification ("ASC") are communicated through

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ADVANCED ENERGY INDUSTRIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

issuance of an Accounting Standards Update (“ASU”). Unless otherwise discussed, we believe that the impact of recently issued guidance, whether adopted or to be adopted in the future, is not expected to have a material impact on the Condensed Consolidated Financial Statements upon adoption.

NOTE 2. BUSINESS ACQUISITION AND DISPOSITION

Acquisition

On May 3, 2010, we acquired PV Powered, a privately-held Oregon corporation based in Bend, Oregon, pursuant to an Agreement and Plan of Merger dated March 24, 2010 between Advanced Energy, PV Powered, and Neptune Acquisition Sub, Inc. (“Acquisition Sub”), an Oregon corporation and wholly-owned subsidiary of Advanced Energy, and Amendment No. 1 to the Agreement and Plan of Merger dated April 21, 2010 (together with the Agreement and Plan of Merger, the “Merger Agreement”). Pursuant to the Merger Agreement, Acquisition Sub merged with and into PV Powered, with PV Powered being the surviving corporation and a wholly-owned subsidiary of Advanced Energy (the “Merger” or “Acquisition”).

PV Powered is a leading manufacturer of grid-tied PV inverters in the residential, commercial and utility-scale markets. PV Powered manufactures high-reliability transformer-based PV inverters utilized in residential, commercial roof top and ground mount systems in the North American market. As of the time of the acquisition, its inverters ranged in size from 30 kilowatts (“kW”) to two megawatts for the commercial market and one kW to five kW for the residential market, all of which had market-leading efficiency ratings.

The PV Powered product line will continue to be assembled in Bend, Oregon although certain sub-assembly manufacturing will be moved to our Shenzhen, China production facility. The acquisition of PV Powered enables us to offer the

solar inverter market a more complete suite of products in wide power ranges and increases the number of solar array opportunities for which our products can be considered for purchase.

Disposition

On October 15, 2010, we completed the sale of our gas flow control business, which includes the Aera[®] mass flow control and related product lines to Hitachi Metals, Ltd. (“Hitachi”), for approximately \$43.3 million. Assets and liabilities sold include, without limitation, inventories, real property in Hachioji, Japan, equipment, certain contracts, intellectual property rights related to the gas flow control business and certain warranty liability obligations.

In connection with the closing of this asset disposition, we entered into a Master Services Agreement and a Supplemental Transition Services Agreement where we will provide certain transition services until October 2011 and we became an authorized service provider for Hitachi in all countries other than Japan. In March 2012, we entered into an agreement to sell certain fixed assets to Hitachi and cease providing contract manufacturing services. We expect this transaction to close in either the second or third quarter of 2012.

In accordance with authoritative accounting guidance for reporting discontinued operations, the results of continuing operations were reduced by the revenue and costs associated with the gas flow control business, which are included in the income from discontinued operations, net of income taxes, in our Condensed Consolidated Statements of Operations.

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ADVANCED ENERGY INDUSTRIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

Operating results of discontinued operations are as follows (in thousands):

	Three Months Ended March 31,	
	2012	2011
Sales	\$4,576	\$6,346
Cost of sales	5,145	6,686
Gross profit	(569	) (340
Operating expenses:		
Research and development	—	8
Selling, general, and administrative	45	50
Total operating expenses	45	58
Operating income (loss) from discontinued operations	(614	) (398
Other income	1,023	611
Income from discontinued operations before income taxes	409	213
Provision for income taxes	106	73
Income from discontinued operations, net of income taxes	\$303	\$140

NOTE 3. INCOME TAXES

The following table sets out the tax expense and the effective tax rate for our income from continuing operations (in thousands):

	Three Months Ended March 31,	
	2012	2011
Provision for income taxes:		
Income from continuing operations before income taxes	\$1,034	\$25,020
Provision for income taxes	268	6,254
Effective tax rate	25.9	% 25.0

Our tax rate is lower than the U.S. federal income tax rate primarily due to the benefit of earnings in foreign jurisdictions, which are subject to lower tax rates. We plan to repatriate approximately \$30.0 million from Japan during the second quarter of 2012, for which a deferred income tax expense of \$2.1 million was recorded in 2010. Other than this planned repatriation, undistributed earnings of foreign subsidiaries are considered to be permanently reinvested and accordingly, no provision for U.S. federal and state income taxes or foreign withholding taxes has been made.

Our policy is to classify accrued penalties and interest related to unrecognized tax benefits in our income tax provision. For the three months ended March 31, 2012 and 2011, the amount of interest and penalties accrued related to our unrecognized tax benefits was immaterial.

NOTE 4. EARNINGS PER SHARE

Basic earnings per share (“EPS”) is computed by dividing income available to common stockholders by the weighted-average number of common shares outstanding during the period. The computation of diluted EPS is similar to the computation of basic EPS except that the numerator is increased to exclude charges that would not have been incurred, and the denominator is increased to include the number of additional common shares that would have been outstanding (using the if-converted and treasury stock methods), if securities containing potentially dilutive common shares (stock options and restricted stock units) had been converted to common shares, and if such assumed conversion is dilutive.

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ADVANCED ENERGY INDUSTRIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The following is a reconciliation of the weighted-average shares outstanding used in the calculation of basic and diluted EPS for the three months ended March 31, 2012 and 2011 (in thousands, except per share data):

	2012	2011
Income from continuing operations, net of income taxes	\$766	\$18,766
Basic weighted-average common shares outstanding	40,781	43,440
Assumed exercise of dilutive stock options and restricted stock units	511	693
Diluted weighted-average common shares outstanding	41,292	44,133
Income from Continuing Operations:		
Earnings per share:		
Basic earnings per share	\$0.02	\$0.43
Diluted earnings per share	\$0.02	\$0.43

The following stock options and restricted units were excluded in the computation of diluted earnings per share because they were anti-dilutive:

	Three months ended March 31,	
	2012	2011
Stock options	5,847	3,311
Restricted stock units	23	—
Total	5,870	3,311

Stock Buyback

In November 2011, our Board of Directors authorized a program to repurchase up to \$75.0 million of our common stock over a twelve month period. Under this program, during the three months ended March 31, 2012, we repurchased and retired 2.0 million shares of our common stock for a total of \$21.9 million. In total, we have repurchased and retired 3.7 million shares of our common stock for a total of \$39.8 million.

All shares repurchased were executed in the open market and no shares were repurchased from related parties.

Repurchased shares were retired and assumed the status of authorized and unissued shares.

NOTE 5. MARKETABLE SECURITIES

Our investments with original maturities of more than three months at time of purchase are considered marketable securities available for sale.

The composition of our marketable securities is as follows (in thousands):

	March 31,		December 31,	
	2012	Fair Value	2011	Fair Value
Commercial paper	\$3,597	\$3,597	\$2,395	\$2,395
Certificates of deposit	8,781	8,781	8,333	8,326
Corporate bonds/notes	8,175	8,176	7,534	7,523
Agency bonds/notes	4,769	4,771	7,320	7,323
Total marketable securities	\$25,322	\$25,325	\$25,582	\$25,567

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ADVANCED ENERGY INDUSTRIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

The maturities of our marketable securities available for sale as of March 31, 2012 are as follows:

	Earliest	to	Latest
Commercial paper	4/26/2012	to	7/23/2012
Certificates of deposit	4/14/2012	to	2/14/2014
Corporate bonds/notes	5/15/2012	to	3/15/2013
Agency bonds/notes	7/15/2012	to	11/2/2012

The value and liquidity of our marketable securities are affected by market conditions, as well as, the ability of the issuer to make principal and interest payments when due, and the functioning of the markets in which these securities are traded. Our current investments in marketable securities are expected to be liquidated during the next twelve months.

As of March 31, 2012, we do not believe any of the underlying issuers of our marketable securities are presently at risk of default.

NOTE 6. DERIVATIVE FINANCIAL INSTRUMENTS

We are impacted by changes in foreign currency exchange rates. We manage these risks through the use of derivative financial instruments, primarily forward contracts. During the three months ended March 31, 2012, we entered into foreign currency exchange forward contracts to manage the exchange rate risk associated with intercompany debt denominated in nonfunctional currencies. These derivative instruments are not designated as hedges; however, they do offset the fluctuations of our intercompany debt due to foreign exchange rate changes.

The notional amount of foreign currency exchange contracts was \$41.5 million at March 31, 2012 and the fair value of these contracts was immaterial at March 31, 2012. During the three months ended March 31, 2012 we recognized \$1.0 million of losses on our foreign currency exchange contracts. These losses were offset by corresponding gains on the related intercompany debt and both are included as a component of other income, net, in our Condensed Consolidated Statements of Operations.

We did not enter into foreign currency forward contracts during the three months ended March 31, 2011.

NOTE 7. ASSETS AND LIABILITIES MEASURED AT FAIR VALUE

Fair Value Hierarchy

Financial assets and liabilities recorded at fair value in our Condensed Consolidated Balance Sheets are categorized based upon a fair value hierarchy established by U.S. GAAP, which prioritizes the inputs used to measure fair value into the following levels:

- Level 1: Quoted market prices in active markets for identical assets or liabilities at the measurement date.
- Level 2: Quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets and liabilities in markets that are not active, or other inputs that are observable and can be corroborated by observable market data.
- Level 3: Inputs reflect management's best estimates and assumptions of what market participants would use in pricing the asset or liability at the measurement date. The inputs are unobservable in the market and significant to the valuation of the instruments.

A financial instrument's categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement.

Assets and Liabilities Measured at Fair Value on a Recurring Basis

The following tables present information about our financial assets measured at fair value, on a recurring basis, as of March 31, 2012, and December 31, 2011. The tables indicate the fair value hierarchy of the valuation techniques utilized to determine such fair value. We did not have any financial liabilities measured at fair value, on a recurring basis, as of March 31, 2012, and December 31, 2011.

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ADVANCED ENERGY INDUSTRIES, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS — (Continued)

March 31, 2012	Level 1 (In thousands)	Level 2	Level 3	Total
Commercial paper	\$—	\$3,597	\$—	\$3,597
Certificates of deposit	—	8,781	—	8,781
Corporate bonds/notes	8,176	—	—	8,176
Agency bonds/notes	4,771	—	—	4,771
Total	\$12,947	\$12,378	\$—	\$25,325
December 31, 2011	Level 1 (In thousands)	Level 2	Level 3	Total
Commercial paper	\$—	\$2,395	\$	