

Clearfield, Inc.
Form 10-Q
January 29, 2018

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

SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended December 31, 2017

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

Commission File Number 0-16106

Clearfield, Inc.

(Exact name of Registrant as specified in its charter)

Minnesota

(State or other jurisdiction of incorporation or organization)

41-1347235

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

7050 Winnetka Avenue North, Suite 100, Brooklyn Park, Minnesota 55428

(Address of principal executive offices and zip code)

(763) 476-6866

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) 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" (as defined in Rule 12b-2 of the Exchange Act).

Large accelerated filer Accelerated filer Non-accelerated filer

Smaller reporting company Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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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Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class:	Outstanding at January 25, 2018
Common stock, par value \$.01	13,817,859

CLEARFIELD, INC.

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PART I. FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

CLEARFIELD, INC.

CONDENSED BALANCE SHEETS

	(Unaudited) December 31, 2017	(Audited) September 30, 2017
Assets		
Current Assets		
Cash and cash equivalents	\$20,453,030	\$18,536,111
Short-term investments	5,385,150	5,937,150
Accounts receivables, net	5,570,721	7,237,641
Inventories	8,140,384	8,453,567
Other current assets	939,326	978,933
Total current assets	40,488,611	41,143,402
Property, plant and equipment, net	5,201,901	5,434,172
Other Assets		
Long-term investments	20,357,000	19,816,000
Goodwill	2,570,511	2,570,511
Other	552,331	529,952
Total other assets	23,479,842	22,916,463
Total Assets	\$69,170,354	\$69,494,037
Liabilities and Shareholders' Equity		
Current Liabilities		
Accounts payable	1,205,223	1,739,791
Accrued compensation	1,443,883	2,410,026
Accrued expenses	98,569	93,304
Total current liabilities	2,747,675	4,243,121
Other Liabilities		
Deferred taxes	60,076	444,076
Deferred rent	279,642	281,720
Total other liabilities	339,718	725,796

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Total Liabilities	3,087,393	4,968,917
Commitments and Contingencies		
Shareholders' Equity		
Preferred stock, \$.01 par value; 500,000 shares; no shares issued or outstanding	-	-
Common stock, authorized 50,000,000, \$.01 par value; 13,824,191 and 13,812,821, shares issued and outstanding at December 31, 2017 and September 30, 2017	138,242	138,128
Additional paid-in capital	56,021,457	55,406,888
Retained earnings	9,923,262	8,980,104
Total Shareholders' Equity	66,082,961	64,525,120
Total Liabilities and Shareholders' Equity	\$69,170,354	\$69,494,037

SEE ACCOMPANYING NOTES TO CONDENSED FINANCIAL STATEMENTS

CLEARFIELD, INC.

CONDENSED STATEMENTS OF EARNINGS

UNAUDITED

	Three Months Ended December 31,	
	2017	2016
Net sales	\$ 16,866,884	\$ 18,266,162
Cost of sales	9,758,477	11,057,442
Gross profit	7,108,407	7,208,720
Operating expenses		
Selling, general and administrative	6,463,971	6,017,524
Income from operations	644,436	1,191,196
Interest income	95,722	52,734
Income before income taxes	740,158	1,243,930
Income tax (benefit) expense	(203,000)	367,000
Net income	\$943,158	\$876,930
Net income per share:		
Basic	\$0.07	\$0.06
Diluted	\$0.07	\$0.06
Weighted average shares outstanding:		
Basic	13,443,945	13,567,484
Diluted	13,476,417	13,790,793

SEE ACCOMPANYING NOTES TO CONDENSED FINANCIAL STATEMENTS

CLEARFIELD, INC.

CONDENSED STATEMENTS OF CASH FLOWS

UNAUDITED

	Three Months Ended December 31,	
	2017	2016
Cash flows from operating activities		
Net income	\$943,158	\$876,930
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	436,198	388,625
Deferred taxes	(384,000)	-
Loss on disposal of assets	1,594	-
Stock based compensation	483,287	593,746
Changes in operating assets and liabilities:		
Accounts receivable	1,666,920	548,293
Inventories	313,183	(341,490)
Other assets	41,706	228,259
Accounts payable, accrued expenses and deferred rent	(1,497,524)	(2,899,667)
Net cash provided by (used in) operating activities	2,004,522	(605,304)
Cash flows from investing activities		
Purchases of property, plant and equipment and intangible assets	(229,999)	(529,302)
Purchases of investments	(2,466,000)	(7,440,000)
Proceeds from maturities of investments	2,477,000	2,459,000
Net cash used in investing activities	(218,999)	(5,510,302)
Cash flows from financing activities		
Repurchases of common stock	(10,850)	-
Proceeds from issuance of common stock under employee stock purchase plan	148,259	169,500
Proceeds from issuance of common stock upon exercise of stock options	3,249	17
Tax withholding related to vesting of restricted stock grants	(9,262)	(10,326)
Net cash provided by financing activities	131,396	159,191
Increase (decrease) in cash and cash equivalents	1,916,919	(5,956,415)
Cash and cash equivalents, beginning of period	18,536,111	28,014,321
Cash and cash equivalents, end of period	\$20,453,030	\$22,057,906
Supplemental disclosures for cash flow information		
Cash paid during the year for income taxes	\$2,500	\$12,250

Non-cash financing activities		
Cashless exercise of stock options	\$5,782	\$32,984

SEE ACCOMPANYING NOTES TO CONDENSED FINANCIAL STATEMENTS

NOTES TO CONDENSED FINANCIAL STATEMENTS

Note 1. Basis of Presentation

The accompanying (a) condensed balance sheet as of September 30, 2017, which has been derived from audited financial statements, and (b) unaudited interim condensed financial statements as of and for the three months ended December 31, 2017 have been prepared by the Company in accordance with accounting principles generally accepted in the United States of America for interim financial information, pursuant to the rules and regulations of the Securities and Exchange Commission. Pursuant to these rules and regulations, certain financial information and footnote disclosures normally included in the financial statements have been condensed or omitted. However, in the opinion of management, the financial statements include all adjustments, consisting of normal recurring accruals, necessary for a fair presentation of the financial position and results of operations and cash flows of the interim periods presented. Operating results for the interim periods presented are not necessarily indicative of results to be expected for the full year or for any other interim period, due to variability in customer purchasing patterns and seasonal, operating and other factors. These condensed financial statements should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended September 30, 2017.

In preparation of the Company's financial statements, management is required to make estimates and assumptions that affect reported amounts of assets and liabilities and related revenues and expenses during the reporting periods. As future events and their effects cannot be determined with precision, actual results could differ significantly from these estimates.

Note 2. Net Income Per Share

Basic net income per common share ("EPS") is computed by dividing net income by the weighted average number of common shares outstanding for the reporting period. Diluted EPS equals net income divided by the sum of the weighted average number of shares of common stock outstanding plus all additional common stock equivalents, such as stock options and restricted stock awards, when dilutive.

The following is a reconciliation of the numerator and denominator of the net income per common share computations for the three months ended December 31, 2017 and 2016:

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	Three Months Ended	
	December 31,	
	2017	2016
Net income	\$943,158	\$876,930
Weighted average common shares	13,443,945	13,567,484
Dilutive potential common shares	32,472	223,309
Weighted average dilutive common shares outstanding	13,476,417	13,790,793
Net income per common share:		
Basic	\$0.07	\$0.06
Diluted	\$0.07	\$0.06

Note 3. Cash, Cash Equivalents and Investments

The Company currently invests its excess cash in money market accounts and bank certificates of deposit (CDs) with a term of not more than five years. CDs with original maturities of more than three months are reported as held-to-maturity investments and are carried at amortized cost. Investments maturing in less than one year are classified as short term investments on the balance sheet, and investments maturing in one year or greater are classified as long term investments on the balance sheet. The maturity dates of the Company's CDs as of December 31, 2017 and September 30, 2017 are as follows:

	December 31, 2017	September 30, 2017
Less than one year	\$5,385,150	\$5,937,150
1-5 years	20,357,000	19,816,000
Total	\$25,742,150	\$25,753,150

Note 4. Stock Based Compensation

The Company recorded \$483,287 of compensation expense related to current and past restricted stock grants and the Company's Employee Stock Purchase Plan ("ESPP") for the three months ended December 31, 2017 of which \$441,257 is included in selling, general and administrative expense, and \$42,030 is included in cost of sales. The Company recorded \$593,746 of compensation expense related to current and past equity awards for the three months ended December 31, 2016 of which \$539,046 was included in selling, general and administrative expense, and \$54,700 was included in cost of sales. As of December 31, 2017, \$4,431,952 of total unrecognized compensation expense related to non-vested restricted stock awards is expected to be recognized over a period of approximately 6.8 years.

There were no stock options granted during the three months ended December 31, 2017 and December 31, 2016. The following is a summary of stock option activity during the three months ended December 31, 2017:

	Number of options	Weighted average exercise price
Outstanding as of September 30, 2017	38,950	\$ 2.79
Granted	-	-
Exercised	(3,500)	2.58
Cancelled or Forfeited	-	-
Outstanding as of December 31, 2017	35,450	\$ 2.81

The intrinsic value of an option is the amount by which the fair value of the underlying stock exceeds its exercise price. As of December 31, 2017, the weighted average remaining contractual term for all outstanding and exercisable stock options was 2.5 years and their aggregate intrinsic value was \$334,810. During the three months ended December 31, 2017, the Company received proceeds of \$3,249 from the exercise of stock options. During the three months ended December 31, 2016, exercised stock options totaled 10,000 shares, resulting in \$17 of proceeds to the Company.

Restricted Stock

The Company's 2007 Stock Compensation Plan permits its Compensation Committee to grant stock-based awards, including stock options and restricted stock, to key employees and non-employee directors. The Company has made restricted stock grants that vest over one to ten years.

There were no restricted stock awards granted during the three months ended December 31, 2017 and December 31, 2016. Restricted stock transactions during the three months ended December 31, 2017 are summarized as follows:

	Number of shares	Weighted average grant date fair value
Unvested shares as of September 30, 2017	370,530	\$ 15.24
Granted	-	-
Vested	(2,000)	13.59
Forfeited	(4,376)	15.46
Unvested as of December 31, 2017	364,154	\$ 15.25

Employee Stock Purchase Plan

Clearfield, Inc.'s ESPP allows participating employees to purchase shares of the Company's common stock at a discount through payroll deductions. The ESPP is available to all employees subject to certain eligibility requirements. Terms of the ESPP provide that participating employees may purchase the Company's common stock on a voluntary after-tax basis. Employees may purchase the Company's common stock at a price that is no less than the lower of 85% of the fair market value of one share of common stock at the beginning or end of each stock purchase period or phase. The ESPP is carried out in six month phases, with phases beginning on January 1 and July 1 of each calendar year. For the phases that ended on December 31, 2017 and December 31, 2016, employees purchased 14,242 and 11,144 shares at a price of \$10.41 and \$15.21 per share, respectively. After the employee purchase on December 31, 2017, 103,013 shares of common stock were available for future purchase under the ESPP.

Note 5. Accounts Receivable

Credit is extended based on the evaluation of a customer's financial condition and collateral is generally not required. Accounts that are outstanding longer than the contractual payment terms are considered past due. The Company writes off accounts receivable when they become uncollectible; payments subsequently received on such receivables are credited to the allowance for doubtful accounts. As of both December 31, 2017 and September 30, 2017, the balance in the allowance for doubtful accounts was \$79,085.

See Note 7, "Major Customer Concentration" for further information regarding accounts receivable and net sales.

Note 6. Inventories

Inventories consist of the following as of:

	December 31, 2017	September 30, 2017
Raw materials	\$6,012,095	\$5,991,863
Work-in-progress	431,495	724,248
Finished goods	1,696,794	1,737,456
Inventories	\$8,140,384	\$8,453,567

During the quarter ended December 31, 2017, the Company adopted Accounting Standards Update ("ASU") 2015-11, *Inventory (Topic 330) Related to Simplifying the Measurement of Inventory* which applies to all inventory except inventory that is measured using last-in, first-out or the retail inventory method. This adoption had no effect on the financial statements and was applied prospectively. Therefore, prior periods were not retrospectively adjusted.

Note 7. Major Customer Concentration

The following table summarizes customers comprising 10% or more of net sales for the three months ended December 31, 2017 and December 31, 2016:

	Three	
	Months	
	Ended	
	December	
	31,	
	2017	2016
Customer A	22%	28%
Customer B	12%	14%

As of December 31, 2017, Customers A and B accounted for 15% and 14% of accounts receivable, respectively. As of September 30, 2017, Customer B accounted for 19% of accounts receivable. Customers A and B are both distributors.

Note 8. Goodwill and Patents

The Company analyzes its goodwill for impairment annually or at an interim period when events occur or changes in circumstances indicate potential impairment. The result of the analysis performed in the fourth quarter ended September 30, 2017 did not indicate an impairment of goodwill. During the quarter ended December 31, 2017, there were no triggering events that indicate potential impairment exists.

The Company capitalizes legal costs incurred to obtain patents. Once accepted by either the U.S. Patent Office or the equivalent office of a foreign country, these legal costs are amortized using the straight-line method over the remaining estimated lives, not exceeding 20 years. As of December 31, 2017, the Company has 12 patents granted and multiple pending applications both inside and outside the United States.

Note 9. Income Taxes

For the three months ended December 31, 2017, the Company recorded a benefit for income taxes of \$203,000, reflecting an effective tax rate of negative 27.4%. The Tax Cut and Jobs Act of 2017 (the "Tax Reform Act") was enacted on December 22, 2017. The Tax Reform Act reduced certain federal corporate income tax rates effective January 1, 2018 and changed certain other provisions. The effective tax rate for the quarter ended December 31, 2017 is a blended rate reflecting the anticipated benefit of three quarters of federal tax rate reductions for fiscal 2018. Our first quarter tax benefit reflects a lower tax rate and a one