BENCHMARK ELECTRONICS INC
Form 10-Q
November 08, 2007

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended September 30, 2007.

o 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: 1-10560

BENCHMARK ELECTRONICS, INC.

(Exact name of registrant as specified in its charter)

Texas (State or other jurisdiction of incorporation or organization)	**74-2211011** (I.R.S. Employer Identification No.)
3000 Technology Drive **Angleton, Texas** (Address of principal executive offices)	**77515** (Zip Code)

(979) 849-6550

(Registrant s telephone number, including area code)

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 x No o

Indicate by check mark whether the registrant is a large accelerated filer, or a non-accelerated filer. See definition of large accelerated filer and non-accelerated filer in Rule 12b 2 of the Act.

Large accelerated filer x Accelerated filer o Non-accelerated filer o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b 2 of the Act). Yes o No x

As of November 7, 2007 there were 71,512,859 Common Shares of Benchmark Electronics, Inc., par value $0.10 per share, outstanding.

PART I FINANCIAL INFORMATION

Item 1. Financial Statements

BENCHMARK ELECTRONICS, INC. AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

(in thousands, except par value)		September 30, 2007 (unaudited)		December 31, 2006
Assets				
Current assets:				
Cash and cash equivalents	$	163,581	$	123,872
Short-term investments		215,440		100,460
Accounts receivable, net of allowance for doubtful accounts of $1,143 and $1,430, respectively		450,703		462,953
Inventories, net		382,474		420,347
Prepaid expenses and other assets		79,238		56,444
Income taxes receivable		3,091		
Deferred income taxes		17,399		6,534
Total current assets		1,311,926		1,170,610
Property, plant and equipment, net of accumulated depreciation of $232,462 and $210,669 respectively		150,905		110,912
Goodwill, net		283,386		112,999
Other, net		29,138		11,599
	$	1,775,355	$	1,406,120
Liabilities and Shareholders Equity				
Current liabilities:				
Notes payable and current installments of long-term debt and capital lease obligations	$	600	$	
Accounts payable		344,676		335,470
Income taxes payable				31,300
Accrued liabilities		57,930		42,948
Total current liabilities		403,206		409,718
Long-term debt and capital lease obligations, less current installments		12,179		
Other long-term liabilities		31,575		2,306
Deferred income taxes		13,143		9,074
Shareholders equity:				
Preferred shares, $0.10 par value; 5,000 shares authorized, none issued				
Common shares, $0.10 par value; 145,000 shares authorized; issued 73,139 and 64,862, respectively; outstanding 73,028 and 64,751, respectively		7,303		6,475
Additional paid-in capital		818,970		586,349
Retained earnings		489,467		398,949
Accumulated other comprehensive loss		(216)		(6,479)
Less treasury shares, at cost; 111 shares		(272)		(272)
Total shareholders equity		1,315,252		985,022
Commitments and contingencies				
	$	1,775,355	$	1,406,120

See accompanying notes to condensed consolidated financial statements.

BENCHMARK ELECTRONICS, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Income

(unaudited)

(in thousands, except per share data)	**Three Months Ended September 30, 2007**	**Three Months Ended September 30, 2006**	**Nine Months Ended September 30, 2007**	**Nine Months Ended September 30, 2006**
Sales	$ 672,595	$ 769,549	$ 2,181,372	$ 2,169,964
Cost of sales	633,818	717,290	2,033,612	2,020,039
Gross profit	38,777	52,259	147,760	149,925
Selling, general and administrative expenses	21,999	17,208	69,466	51,987
Amortization of intangibles	447		1,341	
Restructuring charges and integration costs	1,451	448	7,001	4,478
Income from operations	14,880	34,603	69,952	93,460
Interest expense	(411)	(85)	(1,786)	(268)
Other income	3,831	1,838	9,133	5,508
Income before income taxes	18,300	36,356	77,299	98,700
Income tax expense (benefit)	(3,709)	7,020	4,893	15,318
Net income	$ 22,009	$ 29,336	$ 72,406	$ 83,382
Earnings per share:				
Basic	$ 0.30	$ 0.45	$ 1.00	$ 1.30
Diluted	$ 0.30	$ 0.45	$ 0.99	$ 1.28
Weighted-average number of shares outstanding:				
Basic	72,951	64,585	72,314	64,172
Diluted	73,626	65,492	73,313	65,203

See accompanying notes to condensed consolidated financial statements.

BENCHMARK ELECTRONICS, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Comprehensive Income

(unaudited)

(in thousands)	**Three Months Ended September 30, 2007**	**2006**	**Nine Months Ended September 30, 2007**	**2006**
Net income	$ 22,009	$ 29,336	$ 72,406	$ 83,382
Other comprehensive income:				
Foreign currency translation adjustments	2,793	407	6,263	1,464
Comprehensive income	$ 24,802	$ 29,743	$ 78,669	$ 84,846

Accumulated unrealized foreign currency translation losses were $0.1 million and $6.4 million at September 30, 2007 and December 31, 2006. Foreign currency translation adjustments consist of adjustments to consolidate subsidiaries that use the local currency as their functional currency and transaction gains and losses related to intercompany dollar-denominated debt that is not expected to be repaid in the foreseeable future.

See accompanying notes to condensed consolidated financial statements.

BENCHMARK ELECTRONICS, INC. AND SUBSIDIARIES

Condensed Consolidated Statement of Shareholders Equity

(unaudited)

(in thousands)	Shares	Common shares	Additional paid-in capital	Retained earnings	Accumulated other comprehensive income (loss)	Treasury shares	Total shareholders equity
Balances, December 31, 2006	64,751	$ 6,475	586,349	398,949	(6,479)	(272)	985,022
Adoption of FIN 48				19,335			19,335
Stock-based compensation expense			2,440				2,440
Merger	7,302	730	215,240				215,970
Conversion of debt	351	35	4,965				5,000
Shares repurchased and retired	(109)	(11)	(1,173)	(1,223)			(2,407)
Stock options exercised	733	74	8,719				8,793
Federal tax benefit of stock options exercised			2,430				2,430
Comprehensive income				72,406	6,263		78,669
Balances, September 30, 2007	73,028	$ 7,303	818,970	489,467	(216)	(272)	1,315,252

See accompanying notes to condensed consolidated financial statements.

BENCHMARK ELECTRONICS, INC. AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows

(unaudited)

(in thousands)	**Nine Months Ended September 30, 2007**	**2006**
Cash flows from operating activities:		
Net income	$ 72,406	$ 83,382
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation and amortization	32,003	19,959
Deferred income taxes	7,256	1,462
(Gain) loss on the sale of property, plant and equipment	(511)	9
Asset impairment	273	
Stock-based compensation expense	2,440	2,283
Federal tax benefit of stock options exercised	795	1,250
Changes in operating assets and liabilities, net of effects from acquisitions:		
Accounts receivable	146,553	(84,674)
Inventories	113,795	(170,238)
Prepaid expenses and other assets	7,030	(17,229)
Accounts payable	(123,155)	108,439
Accrued liabilities	(26,058)	6,913
Income taxes	(6,094)	(3,800)
Net cash provided by (used in) operations	226,733	(52,244)
Cash flows from investing activities:		
Purchases of short-term investments	(375,850)	(348,525)
Proceeds from sales and maturities of short-term investments	260,870	413,575
Additions to property, plant and equipment	(12,257)	(28,082)
Proceeds from the sale of property, plant and equipment	1,889	515
Other	400	
Additions to purchased software	(1,626)	(2,246)
Net cash acquired in acquisitions	181	
Net cash provided by (used in) investing activities	(126,393)	35,237
Cash flows from financing activities:		
Proceeds from stock options exercised	8,793	14,710
Federal tax benefit of stock options exercised	1,635	4,787
Principal payments on long-term debt and capital lease obligations	(88,657)	
Proceeds from long-term debt	16,760	
Share repurchases	(2,407)	
Stock split costs		(66)
Net cash provided by (used in) financing activities	(63,876)	19,431
Effect of exchange rate changes	3,245	771
Net increase in cash and cash equivalents	39,709	3,195
Cash and cash equivalents at beginning of year	123,872	110,845
Cash and cash equivalents at September 30	$ 163,581	$ 114,040

See accompanying notes to condensed consolidated financial statements.

BENCHMARK ELECTRONICS, INC. AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(amounts in thousands, except per share data, unless otherwise noted)

(unaudited)

Note 1 - Basis of Presentation

Benchmark Electronics, Inc. (the Company) is a Texas corporation in the business of manufacturing electronics and provides services to original equipment manufacturers (OEMs) of computers and related products for business enterprises, medical devices, industrial control equipment, testing and instrumentation products and telecommunication equipment. The Company has manufacturing operations located in the Americas, Asia and Europe.

The condensed consolidated financial statements included herein have been prepared by the Company without audit pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC). The financial statements reflect all normal and recurring adjustments which in the opinion of management are necessary for a fair presentation of the financial position, results of operations and cash flows for the interim periods presented. The results of operations for the periods presented are not necessarily indicative of the results to be expected for the full year. The accompanying unaudited condensed consolidated financial statements should be read in conjunction with the financial statements and notes included in the Company s Annual Report on Form 10-K for the year ended December 31, 2006.

Management of the Company has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these financial statements in accordance with generally accepted accounting principles. Actual results could differ from those estimates.

Certain reclassifications of prior period amounts have been made to conform to the current presentation.

Note 2 Acquisitions

Effective January 8, 2007, the Company acquired Pemstar Inc. (Pemstar), a publicly traded electronics manufacturing services (EMS) company headquartered in Rochester, Minnesota (the Merger). Pursuant to the Agreement and Plan of Merger among the Company and Pemstar dated October 16, 2006 (the Merger Agreement), each issued and outstanding share of common stock, par value $0.01 per share, of Pemstar was converted into the right to receive 0.160 of a common share, par value $0.10 per share, of the Company. With the closing of the Merger, Pemstar became a wholly owned subsidiary of the Company. This acquisition expanded the Company s customer base and deepened its engineering and systems integration capabilities.

The aggregate purchase price was $221.5 million, including common shares valued at $202.5 million, stock options and warrants valued at $9.0 million, conversion feature of debt valued at $4.8 million and estimated acquisition costs of $5.2 million. The value of the 7.3 million common shares issued was based on the average market price of the Company s common shares over the 2-day period before and after the terms of the acquisition were agreed to and announced.

As a direct result of the Merger, the Company assumed approximately $89.4 million of indebtedness, including $5 million in convertible senior subordinated notes. Subsequent to the Merger, the Company reduced the assumed debt by $71.9 million. The convertible senior subordinated notes matured on May 1, 2007 and were converted into 0.4 million common shares at the request of the noteholders. Prior to the Merger, the Company had no outstanding debt.

The Company is accounting for the Merger utilizing the accounting principles promulgated by Statement of Financial Accounting Standards (SFAS) Nos. 141 and 142. Therefore, the results of operations of the Pemstar operations since January 8, 2007 have been included in the accompanying consolidated statement of income. The preliminary allocation of the net purchase price of the Merger resulted in goodwill of approximately $165.6 million. The ultimate allocation of the purchase price may differ from the amounts included in these financial statements. Adjustments to the purchase price allocations, if any, are expected to be finalized by the end of 2007, and will be reflected in future filings. Management does not expect these adjustments, if any, to have a material effect on the Company s financial position or results of operations. In connection with the Merger, the Company amended its Amended and Restated Credit Agreement dated June 23, 2000 to permit the Merger.

The following is an estimate of the purchase price for Pemstar and the preliminary purchase price allocation:

Acquisition of the 45.6 million shares of outstanding common stock of Pemstar at $4.44 per share	$	202,475
Estimated fair value of Pemstar stock options and warrants		9,028
Estimated fair value of the conversion feature of debt		4,773
Acquisition costs		5,179
Total purchase price	$	221,455
Current assets	$	241,312
Property, plant and equipment		52,542
Deferred taxes		11,286
Goodwill		165,575
Intangible assets		18,277
Other assets		7,151
Total assets acquired		496,143
Current liabilities		182,543
Long-term debt, capital lease obligations and other long-term liabilities		92,145
Total liabilities assumed		274,688
Net assets acquired	$	221,455

On March 1, 2007, we terminated a joint venture agreement and acquired for $5.3 million the remaining 40% minority interest in the Company s Romanian subsidiary. We acquired the other 60% interest in the Merger discussed above. The purchase price in excess of the 40% minority interest liability resulted in goodwill of $4.7 million.

The following summary pro forma condensed consolidated financial information reflects the acquisition of Pemstar as if it had occurred on January 1, 2006 for purposes of the statements of income. The summary pro forma information is not necessarily representative of what the Company s results of operations would have been had the acquisition of Pemstar in fact occurred on January 1, 2006 and is not intended to project the Company s results of operations for any future period or date. Pro forma results of operations for the nine months ended September 30, 2007 related to the Merger have not been presented since the operating results for Pemstar for the period up to the date of acquisition are immaterial.

Pro forma condensed consolidated financial information for the nine months ended September 30, 2006 (unaudited):

		Nine months ended September 30, 2006
Net sales	$	2,582,832
Gross profit	$	190,980
Income from operations	$	110,231
Net income	$	91,154
Earnings per share:		
Basic	$	1.28
Diluted	$	1.25
Weighted-average number of shares outstanding:		
Basic		71,474
Diluted		73,133

Note 3 Stock-Based Compensation

The Company s stock awards plan permits the grant of a variety of types of awards, including stock options, restricted stock awards, stock appreciation rights, performance awards, and phantom stock awards, or any combination thereof, to key employees of the Company. Stock options are granted to employees with an exercise price equal to the market price of the Company s stock on the date of grant, vest over a four-year period from the date of grant and have a term of ten years. Members of the Board of Directors of the Company who are not employees of the Company participate in a separate stock option plan that provides for the granting of stock options upon the occurrence of the non-employee director s election or re-election to the Board of Directors. All awards under the non-employee director stock option plan are fully vested upon the date of grant and have a term of ten years. As of September 30, 2007, 5.6 million additional options may be granted under the Company s existing plans.

Statement of Financial Accounting Standards (SFAS) No. 123 (revised 2004), Share-Based Payment (SFAS No. 123R) requires all share-based payments to employees, including grants of employee stock options, to be recognized in the financial statements based on their fair values. The total compensation cost recognized for stock-option awards was $0.6 million and $2.4 million for the three and nine month periods ended September 30, 2007, and $0.6 million and $2.3 million for the three and nine month periods ended September 30, 2006. The compensation expense for stock-based awards includes an estimate for forfeitures and is recognized over the vesting period of the options using the straight-line method. SFAS No. 123R requires that cash flows from the tax benefits resulting from tax deductions in excess of the compensation cost recognized for stock-based awards (excess tax benefits) be classified as cash flows from financing activities.

As of September 30, 2007, there was approximately $6.5 million of total unrecognized compensation cost related to nonvested stock options. That cost is expected to be recognized over a weighted-average period of 2.6 years.

The Company did not issue any options during the three months ended September 30, 2007. During the nine months ended September 30, 2007, the Company issued 0.4 million options. In connection with the Merger, all outstanding Pemstar options were converted into options of the Company at the 0.160 exchange ratio on January 8, 2007. These were the only options issued during the three months ended March 31, 2007. During the three and nine months ended September 30, 2006, the Company issued 15 thousand and 1.1 million options, respectively. The fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model. The weighted-average assumptions used to value the options converted from Pemstar and the option grants during the three and nine months ended September 30, 2007 and 2006 were as follows:

	Three Months Ended September 30,		**Nine Months Ended September 30,**	
	2007	**2006**	**2007**	**2006**
Expected term of options		6.0 years	2.7 years	4.5 years
Expected volatility		44%	29%	46%
Risk-free interest rate		4.75%	4.83%	4.43%
Dividend yield		zero	zero	zero

The expected term of the options represents the estimated period of time until exercise and is based on historical experience, giving consideration to the contractual terms, vesting schedules and expectations of future employee behavior. Separate groups of employees that have similar historical exercise behavior are considered separately for valuation purposes. Expected stock price volatility is based on the historical volatility of the Company s stock. The risk-free interest rate is based on the U.S. Treasury zero-coupon rates in effect at the time of grant with an equivalent remaining term. The dividend yield reflects that the Company has not paid any cash dividends since inception.

The weighted-average fair value per option granted during the nine months ended September 30, 2007 was $9.46. The total cash received as a result of stock option exercises for the nine months ended September 30, 2007 and 2006 was approximately $8.8 million and $14.7 million, respectively. The tax benefit realized as a result of the stock option exercises was $2.4 million and $6.0 million during the first nine months of 2007 and 2006. For the nine months ended September 30, 2007 and 2006, the total intrinsic value of stock options exercised was $7.7 million and $19.5 million, respectively.

The following table summarizes the activities relating to the Company s stock option plans:

	Number of Options		**Weighted-Average Exercise Price**	**Weighted-Average Remaining Contractual Term (Years)**	**Aggregate Intrinsic Value**
Outstanding at December 31, 2006	5,716	$	18.54	6.37	
Granted	51	$	21.35		
Converted from Merger	369	$	25.47		
Exercised	(733)	$	11.99		
Canceled	(209)	$	29.91		