

HURCO COMPANIES INC  
Form 10-Q  
June 03, 2011

UNITED STATES  
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 April 30, 2011 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 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 small 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  (Do not check if a smaller reporting company)

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

The number of shares of the Registrant's common stock outstanding as of June 1, 2011 was 6,440,851.

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HURCO COMPANIES, INC.  
April 2011 Form 10-Q Quarterly Report

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## PART I - FINANCIAL INFORMATION

## Item 1. FINANCIAL STATEMENTS

HURCO COMPANIES, INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS  
 (In thousands, except per share data)

	Three Months Ended April 30		Six Months Ended April 30	
	2011	2010	2011	2010
	(Unaudited)		(Unaudited)	
Sales and service fees	\$41,576	\$24,088	\$81,256	\$44,704
Cost of sales and service	28,925	19,411	56,914	36,047
Gross profit	12,651	4,677	24,342	8,657
Selling, general and administrative expenses	9,254	7,230	18,084	13,763
Operating income (loss)	3,397	(2,553 )	6,258	(5,106 )
Interest expense	9	8	14	22
Interest income	32	5	72	25
Investment income	2	3	7	8
Other (income) expense, net	23	116	479	393
Income (loss) before taxes	3,399	(2,669 )	5,844	(5,488 )
Provision (benefit) for income taxes	1,050	(1,096 )	1,949	(2,079 )
Net income (loss)	\$2,349	\$(1,573 )	\$3,895	\$(3,409 )
Income (losses) per common share				
Basic	\$.36	\$(0.24 )	\$.60	\$(0.53 )
Diluted	\$.36	\$(0.24 )	\$.60	\$(0.53 )
Weighted average common shares outstanding				
Basic	6,441	6,441	6,441	6,441
Diluted	6,489	6,441	6,476	6,441

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



HURCO COMPANIES, INC.  
CONDENSED CONSOLIDATED BALANCE SHEETS  
(In thousands, except share and per-share data)

	April 30 2011 (Unaudited)	October 31 2010 (Audited)
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$48,678	\$48,255
Accounts receivable, net	24,175	20,114
Refundable taxes	4,387	5,093
Inventories, net	69,610	55,866
Deferred income taxes	2,965	2,467
Derivative assets	1,530	905
Other	5,458	3,508
Total current assets	156,803	136,208
Non-current assets:		
Property and equipment:		
Land	782	782
Building	7,116	7,116
Machinery and equipment	15,901	15,095
Leasehold improvements	2,334	2,183
	26,133	25,176
Less accumulated depreciation and amortization	(14,804 )	(13,424 )
	11,329	11,752
Software development costs, less accumulated amortization	5,588	6,042
Investments and other assets, net	6,268	6,344
	\$179,988	\$160,346
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$38,745	\$30,394
Accrued expenses and other	10,482	8,132
Accrued warranty expenses	1,778	1,591
Derivative liabilities	4,230	2,123
Short-term debt	647	—
Total current liabilities	55,882	42,240
Non-current liabilities:		
Deferred income taxes	2,440	2,335
Deferred credits and other	1,152	1,031
Total liabilities	59,474	45,606
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, 13,250,000 shares authorized, 6,471,710 and 6,440,851 shares issued; and 6,440,851 and 6,440,851 shares outstanding,	644	644

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as of April 30, 2011 and October 31, 2010, respectively

Additional paid-in capital	52,338	52,144
Retained earnings	67,719	63,824
Accumulated other comprehensive loss	(187 )	(1,872 )
Total shareholders' equity	120,514	114,740
	\$ 179,988	\$ 160,346

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

HURCO COMPANIES, INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 (In thousands)

	Three Months Ended April 30		Six Months Ended April 30	
	2011	2010	2011	2010
	(Unaudited)		(Unaudited)	
<b>Cash flows from operating activities:</b>				
Net income (loss)	\$2,349	\$(1,573 )	\$3,895	\$(3,409 )
Adjustments to reconcile net income (loss) to net cash provided by (used for) operating activities:				
Provision for doubtful accounts	(256 )	(74 )	(202 )	(189 )
Deferred income taxes	110	(243 )	230	(783 )
Equity in (income) loss of affiliates	(22 )	69	(17 )	181
Depreciation and amortization	1,079	1,000	2,146	1,833
Foreign currency (gain) loss	(3,306 )	1,365	(3,320 )	3,584
Unrealized (gain) loss on derivatives	(422 )	(173 )	(288 )	(835 )
Stock-based compensation	123	31	194	49
<b>Change in assets and liabilities:</b>				
(Increase) decrease in accounts receivable and refundable taxes	(4,364 )	(1,609 )	(2,084 )	(403 )
(Increase) decrease in inventories	(7,863 )	2,135	(10,831 )	7,413
Increase (decrease) in accounts payable	8,376	4,876	6,622	4,649
Increase (decrease) in accrued expenses	(152 )	(336 )	1,765	(1,067 )
Net change in derivative assets and liabilities	1,044	(1 )	587	(1,039 )
Other	845	(1,042 )	1,201	(848 )
Net cash provided by (used for) operating activities	(2,459 )	4,425	(102 )	9,136
<b>Cash flows from investing activities:</b>				
Proceeds from sale of property and equipment	—	35	—	35
Purchase of property and equipment	(207 )	(67 )	(375 )	(249 )
Software development costs	(279 )	(202 )	(652 )	(495 )
Other investments	28	(8 )	16	(17 )
Net cash provided by (used for) investing activities	(458 )	(242 )	(1,011 )	(726 )
<b>Cash flows from financing activities:</b>				
Advances on short-term debt	637	—	637	—
Effect of exchange rate changes on cash	669	(546 )	899	(1,174 )
Net increase (decrease) in cash and cash equivalents	(1,611 )	3,637	423	7,236
Cash and cash equivalents at beginning of period	50,289	32,381	48,255	28,782
Cash and cash equivalents at end of period	\$48,678	\$36,018	\$48,678	\$36,018

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





HURCO COMPANIES, INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY  
 For the six months ended April 30, 2011 and 2010  
 (Unaudited)

(In thousands, except shares outstanding)	Common stock		Additional	Retained	Accumulated other comprehensive income (loss)	Total
	Shares outstanding	Amount	paid-in capital	earnings		
Balances, October 31, 2009	6,440,851	\$644	\$52,003	\$69,568	\$ (1,839 )	\$120,376
Net loss	—	—	—	(3,409 )	—	(3,409 )
Translation of foreign currency financial statements	—	—	—	—	(1,617 )	(1,617 )
Realized loss on derivative instruments reclassified into operations, net of tax of \$46	—	—	—	—	75	75
Unrealized gain on derivative instruments, net of tax of \$533	—	—	—	—	865	865
Comprehensive loss	—	—	—	—	—	(4,086 )
Stock-based compensation expense	—	—	49	—	—	49
Balances, April 30, 2010 (Unaudited)	6,440,851	\$644	\$52,052	\$66,159	\$ (2,516 )	\$116,339
Balances, October 31, 2010	6,440,851	\$644	\$52,144	\$63,824	\$ (1,872 )	\$114,740
Net income	—	—	—	3,895	—	3,895
Translation of foreign currency financial statements	—	—	—	—	2,888	2,888
Realized gain on derivative instruments reclassified into operations, net of tax of \$(184)	—	—	—	—	( 313 )	(313 )
Unrealized loss on derivative instruments, net of tax of \$(523)	—	—	—	—	(890 )	(890 )
Comprehensive income	—	—	—	—	—	5,580

Stock-based compensation expense	—	—	194	—	—	194
Balances, April 30, 2011 (Unaudited)	6,440,851	\$644	\$52,338	\$67,719	\$ (187 )	\$120,514

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 April 30, 2011 and for the three and six months ended April 30, 2011 and April 30, 2010 is unaudited; however, in our opinion, the interim data includes all adjustments, consisting only of normal recurring adjustments, necessary to present fairly our consolidated financial position, results of operations, changes in shareholders’ equity and cash flows 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, 2010.

2. DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

We are exposed to certain market risks relating to our ongoing business operations, including foreign currency risk, interest rate risk and credit risk. We manage our exposure to these and other market risks through regular operating and financing activities. Currently, the only risk that we manage through the use of derivative instruments is foreign currency risk.

We operate on a global basis and are exposed to the risk that our financial condition, results of operations and cash flows could be adversely affected by changes in foreign currency exchange rates. To reduce the potential effects of foreign exchange rate movements on our net equity investment in one of our foreign subsidiary’s gross profit and net earnings, we enter into derivative financial instruments in the form of foreign exchange forward contracts with a major financial institution. We are primarily exposed to foreign currency exchange rate risk with respect to transactions and net assets denominated in Euros, Pounds Sterling, Canadian Dollars, South African Rand, Singapore Dollars and New Taiwan Dollars.

We record all derivative instruments as assets or liabilities at fair value.

Derivatives Designated as Hedging Instruments

We enter into foreign currency forward exchange contracts periodically to hedge certain forecasted inter-company sales and 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 Derivative assets and Derivative liabilities. The effective portion of the gains and losses resulting from the changes in the fair value of these hedge contracts are deferred in Accumulated other comprehensive loss and recognized as an adjustment to Cost of sales and service in the period that the corresponding inventory sold 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. The ineffective portion of gains and losses resulting from the changes in the fair value of

these hedge contracts is reported in Other (income) expense, net immediately. We perform quarterly assessments of hedge effectiveness by verifying and documenting the critical terms of the hedge instrument and determining that forecasted transactions have not changed significantly. We also assess on a quarterly basis whether there have been adverse developments regarding the risk of a counterparty default.

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We had forward contracts outstanding as of April 30, 2011, denominated in Euros, Pounds Sterling and New Taiwan Dollars with set maturity dates ranging from May 2011 through April 2012. The contract amounts, expressed at forward rates in U.S. Dollars at April 30, 2011, were \$38.4 million for Euros, \$10.5 million for Pounds Sterling and \$33.5 million for New Taiwanese Dollars. At April 30, 2011, we had approximately \$1.6 million of losses, net of tax, related to cash flow hedges deferred in Accumulated other comprehensive loss. Of this amount, \$1.4 million represents unrealized losses, net of tax, related to cash flow hedge instruments that remain subject to currency fluctuation risk. The majority of these deferred losses will be recorded as an adjustment to Cost of sales and service in periods through April 2012, when the corresponding inventory that is the subject of the related hedge contract is sold, as described above.

We are also exposed to foreign currency exchange risk related to our investment in net assets in foreign countries. To manage this risk, we have maintained a forward contract with a notional amount of €3.0 million. We designated this forward contract as a hedge of our net investment in Euro denominated assets. We selected the forward method under FASB guidance related to the accounting for derivatives instruments and hedging activities. The forward method requires all changes in the fair value of the contract to be reported as a cumulative translation adjustment in Accumulated other comprehensive loss, net of tax, in the same manner as the underlying hedged net assets. This forward contract matures in November 2011. At April 30, 2011, we had \$216,000 of realized gains and \$226,000 of unrealized losses, net of tax, recorded as cumulative translation adjustments in Accumulated other comprehensive loss related to this forward contract.

#### Derivatives Not Designated as Hedging Instruments

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 guidance of the Financial Accounting Standards Board, or FASB, and, as a result, changes in their fair value are reported currently as Other (income) expense, net in the Condensed Consolidated Statements of Operations consistent with the transaction gain or loss on the related receivables and payables denominated in foreign currencies.

We had forward contracts outstanding as of April 30, 2011, in Euros, Pounds Sterling, Canadian Dollars, South African Rand, Singapore Dollars and New Taiwan Dollars with set maturity dates ranging from May 2011 through September 2011. The amounts of these contracts at forward rates in U.S. Dollars at April 30, 2011 for Euros, Pounds Sterling, Canadian Dollars, South African Rand, New Taiwan Dollars and Singapore Dollars totaled \$28.3 million.

## Fair Value of Derivative Instruments

We recognize the fair value of derivative instruments as assets and liabilities on a gross basis on our Condensed Consolidated Balance Sheets. As of April 30, 2011 and October 31, 2010, all derivative instruments were recorded at fair value on the balance sheets as follows (in thousands):

Derivatives	2011 Balance sheet location	Fair value	2010 Balance sheet location	Fair value
<b>Designated as hedging instruments:</b>				
Foreign exchange forward contracts	Derivative assets	\$ 1,306	Derivative assets	\$ 872
Foreign exchange forward contracts	Derivative liabilities	\$ 3,963	Derivative liabilities	\$ 1,778
<b>Not designated as hedging instruments:</b>				
Foreign exchange forward contracts	Derivative assets	\$ 224	Derivative assets	\$ 33
Foreign exchange forward contracts	Derivative liabilities	\$ 267	Derivative liabilities	\$ 345

## Effect of Derivative Instruments on the Condensed Consolidated Balance Sheets and Condensed Consolidated Statements of Changes in Shareholders' Equity and Operations

Derivative instruments had the following effects on our Condensed Consolidated Balance Sheets and Condensed Consolidated Statements of Changes in Shareholders' Equity and Operations during the six months ended April 30, 2011 and 2010 (in thousands):

Derivatives	Amount of gain (loss) recognized in Other comprehensive loss		Location of gain (loss) reclassified from Other comprehensive loss	Amount of gain (loss) reclassified from Other comprehensive loss	
	Six months ended April 30, 2011	2010		Six months ended April 30, 2011	2010
<b>Designated as hedging instruments: (Effective portion)</b>					
Foreign exchange forward contracts			Cost of sales and service		
– Intercompany sales/purchases	\$ (1,413 )	\$ 1,398		\$ 497	\$ (121 )
Foreign exchange forward contract					
– Net investment	\$ (279 )	\$ 401			

We recognized a loss of \$25,000 for the six months ended April 30, 2011, and a loss of \$65,000 for the six months ended April 30, 2010 as a result of contracts closed early that were deemed ineffective for financial reporting purposes.



Derivatives	Location of gain (loss) recognized in operations	Amount of gain (loss) recognized in operations	
		Six months ended April 30, 2011	2010
<b>Not designated as hedging instruments:</b>			
Foreign exchange forward contracts	Other (income) expense, net	\$ (548 )	\$ 1,334

Derivative instruments had the following effects on our Condensed Consolidated Balance Sheets and Condensed Consolidated Statements of Changes in Shareholders' Equity and Operations during the three months ended April 30, 2011 and 2010 (in thousands):

Derivatives	Amount of gain (loss) recognized in Other comprehensive loss
	Three months ended April 30,