

CTS CORP  
Form 10-Q  
October 27, 2010

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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 October 3, 2010

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: 1-4639

CTS CORPORATION

(Exact name of registrant as specified in its charter)

Indiana  
(State or other jurisdiction  
of incorporation or  
organization)

35-0225010  
(IRS Employer  
Identification  
Number)

905 West Boulevard North,  
Elkhart, IN  
(Address of principal executive  
offices)

46514  
(Zip Code)

Registrant's telephone number, including area code: 574-523-3800

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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 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 definition of “large accelerated filer”, “accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer  Non-accelerated filer (Do not check if 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

Indicate the number of shares outstanding of each of the issuer’s classes of common stock, as of October 25, 2010:  
34,183,382.

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CTS CORPORATION AND SUBSIDIARIES

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## PART I - FINANCIAL INFORMATION

## Item 1. Financial Statements

CTS CORPORATION AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS/(LOSS) - UNAUDITED  
 (In thousands, except per share amounts)

	Three Months Ended		Nine Months Ended	
	October 3, 2010	September 27, 2009	October 3, 2010	September 27, 2009
Net sales	\$139,362	\$126,565	\$407,616	\$365,094
Costs and expenses:				
Cost of goods sold	109,393	100,380	316,828	297,202
Selling, general and administrative expenses	17,112	16,494	54,944	48,357
Research and development expenses	5,086	3,408	13,985	10,227
Restructuring charge – Note I	—	—	—	2,243
Goodwill impairment	—	—	—	33,153
Operating earnings/(loss)	7,771	6,283	21,859	(26,088 )
Other (expense)/income:				
Interest expense	(254 )	(256 )	(717 )	(1,615 )
Interest income	105	17	239	118
Other	1,738	(390 )	917	(736 )
Total other income/(expense)	1,589	(629 )	439	(2,233 )
Earnings/(loss) before income taxes	9,360	5,654	22,298	(28,321 )
Income tax expense	2,445	1,173	5,060	9,872
Net earnings/(loss)	\$6,915	\$4,481	\$17,238	\$(38,193 )
Net earnings/(loss) per share - Note J				
Basic	\$0.20	\$0.13	\$0.51	\$(1.13 )
Diluted	\$0.20	\$0.13	\$0.50	\$(1.13 )
Cash dividends declared per share	\$0.03	\$0.03	\$0.09	\$0.09
Average common shares outstanding:				
Basic	34,181	33,873	34,060	33,799
Diluted	34,827	34,513	34,816	33,799

See notes to unaudited condensed consolidated financial statements.

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CTS CORPORATION AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS - UNAUDITED  
(In thousands of dollars)

	October 3, 2010	December 31, 2009
<b>ASSETS</b>		
<b>Current Assets</b>		
Cash and cash equivalents	\$ 73,031	\$ 51,167
Accounts receivable, less allowances (2010 - \$1,705; 2009- \$2,119)	90,136	71,718
Inventories, net - Note D	76,562	54,348
Other current assets	19,325	16,502
<b>Total current assets</b>	<b>259,054</b>	<b>193,735</b>
Property, plant and equipment, less accumulated depreciation (2010 - \$247,564; 2009 - \$264,651)	79,409	81,120
<b>Other Assets</b>		
Prepaid pension asset	32,621	29,373
Goodwill – Note L	500	500
Other intangible assets, net – Note L	32,056	33,938
Deferred income taxes	66,662	68,331
Other	579	660
<b>Total other assets</b>	<b>132,418</b>	<b>132,802</b>
<b>Total Assets</b>	<b>\$ 470,881</b>	<b>\$ 407,657</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current Liabilities</b>		
Accounts payable	\$ 70,534	\$ 52,344
Accrued liabilities	41,201	38,172
<b>Total current liabilities</b>	<b>111,735</b>	<b>90,516</b>
Long-term debt - Note E	77,100	50,400
Other long-term obligations	16,902	19,287
<b>Shareholders' Equity</b>		
Preferred stock - authorized 25,000,000 shares without par value; none issued	—	—
Common stock - authorized 75,000,000 shares without par value; 54,504,141 shares issued		
at October 3, 2010 and 54,213,931 shares issued at December 31, 2009	285,350	282,491
Additional contributed capital	36,886	37,675
Retained earnings	331,750	317,582
Accumulated other comprehensive loss	(91,833)	(93,285)
	562,153	544,463
Cost of common stock held in treasury (2010 and 2009 – 20,320,759 shares)	(297,009)	(297,009)
<b>Total shareholders' equity</b>	<b>265,144</b>	<b>247,454</b>
<b>Total Liabilities and Shareholders' Equity</b>	<b>\$ 470,881</b>	<b>\$ 407,657</b>

See notes to unaudited condensed consolidated financial statements.



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CTS CORPORATION AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS - UNAUDITED  
(In thousands of dollars)

	Nine Months Ended	
	October 3, 2010	September 27, 2009
Cash flows from operating activities:		
Net earnings/(loss)	\$ 17,238	(38,193)
Adjustments to reconcile net earnings/(loss) to net cash provided by operating activities:		
Depreciation and amortization	13,244	14,919
Prepaid pension asset	(5,985)	(5,853)
Equity-based compensation – Note B	2,911	2,711
Restructuring and impairment charges – Note I	—	2,243
Goodwill impairment – Note L	—	33,153
Amortization of retirement benefit adjustments – Note F	3,646	3,942
Other	(987)	7,389
Changes in assets and liabilities, net of acquisitions		
Accounts receivable	(17,929)	20,045
Inventories	(21,587)	11,031
Other current assets	(2,697)	1,600
Accounts payable and accrued liabilities	20,241	(18,936)
Total adjustments	(9,143)	72,244
Net cash provided by operating activities	8,095	34,051
Cash flows from investing activities:		
Earnout payment related to a 2008 acquisition	(500)	—
Capital expenditures	(10,505)	(4,681)
Proceeds from sales of assets	1,530	1,309
Net cash used in investing activities	(9,475)	(3,372)
Cash flows from financing activities:		
Payment of 2.125% Debentures	—	(32,500)
Payments of long-term debt – Note E	(2,488,950)	(2,141,050)
Proceeds from borrowings of long-term debt – Note E	2,515,650	2,142,550
Payments of short-term notes payable	(2,258)	(7,755)
Proceeds from borrowings of short-term notes payable	2,258	7,755
Dividends paid	(3,063)	(3,040)
Other	69	(929)
Net cash provided by/(used in) financing activities	23,706	(34,969)
Effect of exchange rate on cash and cash equivalents	(462)	(9)
Net increase/(decrease) in cash and cash equivalents	21,864	(4,299)
Cash and cash equivalents at beginning of year	51,167	44,628

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Cash and cash equivalents at end of period	\$	73,031	\$	40,329
Supplemental cash flow information				
Cash paid during the period for:				
Interest	\$	633	\$	728
Income taxes—net	\$	2,370	\$	5,915

See notes to unaudited condensed consolidated financial statements.



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CTS CORPORATION AND SUBSIDIARIES  
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE EARNINGS/ (LOSS) - UNAUDITED  
 (In thousands of dollars)

	Three Months Ended		Nine Months Ended	
	October 3, 2010	September 27, 2009	October 3, 2010	September 27, 2009
Net earnings/(loss)	\$ 6,915	\$ 4,481	\$ 17,238	\$ (38,193)
Other comprehensive earnings/(loss):				
Cumulative translation adjustment	1,090	(352)	(546)	1,925
Amortization of retirement benefit adjustments (net of tax)	582	779	1,998	2,253
Comprehensive earnings/(loss)	\$ 8,587	\$ 4,908	\$ 18,690	\$ (34,015)

See notes to unaudited condensed consolidated financial statements.

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NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS - UNAUDITED  
October 3, 2010

## NOTE A – Basis of Presentation

The accompanying condensed consolidated financial statements have been prepared by CTS Corporation (“CTS” or “the Company”) without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been omitted pursuant to such rules and regulations. The unaudited condensed consolidated financial statements should be read in conjunction with the financial statements, notes thereto, and other information included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2009.

The accompanying unaudited condensed consolidated financial statements reflect, in the opinion of management, all adjustments (consisting of normal recurring items) necessary for a fair statement, in all material respects, of the financial position and results of operations for the periods presented. The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reported period. Actual results could differ materially from those estimates. The results of operations for the interim periods are not necessarily indicative of the results for the entire year.

## NOTE B – Equity-Based Compensation

At October 3, 2010, CTS had five equity-based compensation plans: the 1996 Stock Option Plan (“1996 Plan”), the 2001 Stock Option Plan (“2001 Plan”), the Nonemployee Directors’ Stock Retirement Plan (“Directors’ Plan”), the 2004 Omnibus Long-Term Incentive Plan (“2004 Plan”), and the 2009 Omnibus Equity and Performance Incentive Plan (“2009 Plan”). All of these plans, except the Directors’ Plan, were approved by shareholders. As of December 31, 2009, additional grants can only be made under the 2004 and 2009 Plans. CTS believes that equity based awards align the interest of employees with those of its shareholders.

The 2009 Plan, and previously the 1996 Plan, 2001 Plan and 2004 Plan, provides for grants of incentive stock options or nonqualified stock options to officers, key employees, and nonemployee members of CTS’ board of directors. In addition, the 2009 Plan and the 2004 Plan allows for grants of stock appreciation rights, restricted stock, restricted stock units, performance shares, performance units, and other stock awards.

The following table summarizes the compensation expense included in the Unaudited Condensed Consolidated Statements of Earnings/(Loss) for the three and nine months ended October 3, 2010 and September 27, 2009 relating to these plans:

	Three Months Ended		Nine Months Ended	
	October 3 2010	September 27, 2009	October 3, 2010	September 27, 2009
(\$ in thousands)				
Stock options	\$—	\$2	\$3	\$34
Restricted stock units	746	907	2,908	2,677
Total	\$746	\$909	\$2,911	\$2,711

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The following table summarizes the status of these plans as of October 3, 2010:

	2009 Plan	2004 Plan	2001 Plan	1996 Plan
Awards originally available	3,400,000	6,500,000	2,000,000	1,200,000
Stock options outstanding	—	276,850	709,013	128,350
Restricted stock units outstanding	515,494	265,004	—	—
Options exercisable	—	276,850	709,013	128,350
Awards available for grant	2,751,449	268,500	—	—

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## Stock Options

Stock options are exercisable in cumulative annual installments over a maximum 10-year period, commencing at least one year from the date of grant. Stock options are generally granted with an exercise price equal to the market price of the Company's stock on the date of grant. The stock options generally vest over four years and have a 10-year contractual life. The awards generally contain provisions to either accelerate vesting or allow vesting to continue on schedule upon retirement if certain service and age requirements are met. The awards also provide for accelerated vesting if there is a change in control event.

The Company estimates the fair value of the stock option on the grant date using the Black-Scholes option-pricing model and assumptions for expected price volatility, option term, risk-free interest rate, and dividend yield. Expected price volatilities are based on historical volatilities of the Company's stock. The expected option term is derived from historical data on exercise behavior. The dividend yield is based on historical dividend payments. The risk-free rate for periods within the contractual life of the option is based on the U.S. Treasury yield curve in effect at the time of grant.

A summary of the status of stock options as of October 3, 2010 and September 27, 2009, and changes during the nine-month periods then ended, is presented below:

	October 3, 2010		September 27, 2009	
	Options	Weighted-Average Exercise Price	Options	Weighted-Average Exercise Price
Outstanding at beginning of year	1,179,088	\$ 13.72	1,294,263	\$ 14.53
Exercised	(17,000 )	\$ 7.70	—	\$ —
Expired	(47,875 )	\$ 42.30	(109,675 )	\$ 21.45
Forfeited	—	\$ —	—	\$ —
Outstanding at end of period	1,114,213	\$ 12.59	1,184,588	\$ 13.89
Exercisable at end of period	1,114,213	\$ 12.59	1,163,838	\$ 13.89

The total intrinsic value of share options exercised during the nine-month period ended October 3, 2010 was \$30,000. There were no share options exercised during the nine-month period ended September 27, 2009.

The weighted-average remaining contractual life of options outstanding and options exercisable at October 3, 2010 is 2.4 years. The aggregate intrinsic value of options outstanding and options exercisable at October 3, 2010 is approximately \$550,000.

A summary of the nonvested stock options as of October 3, 2010 and September 27, 2009, and changes during the nine-month periods then ended, is presented below:

	October 3, 2010		September 27, 2009	
	Options	Weighted-average Grant-Date Fair Value	Options	Weighted-average Grant-Date Fair Value
Nonvested at beginning of year	20,750	\$ 6.24	74,525	\$ 6.36
Vested	(20,750 )	\$ 6.24	(53,775 )	\$ 6.41
Forfeited	—	\$ —	—	\$ —

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Nonvested at end of period	—	\$ —	20,750	\$ 6.24
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The total fair value of options vested during the nine-month periods ended October 3, 2010 and September 27, 2009 was approximately \$130,000 and \$345,000, respectively. As of October 3, 2010, there was no unrecognized compensation cost related to nonvested stock options. CTS recognized expense on a straight-line basis over the requisite service period for each separately vesting portion of the award as if the award was, in substance, multiple awards.

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The following table summarizes information about stock options outstanding at October 3, 2010:

Range of Exercise Prices	Number Outstanding at 10/3/10	Options Outstanding		Options Exercisable	
		Weighted Average Remaining Contractual Life (Years)	Weighted Average Exercise Price	Number Exercisable At 10/3/10	Weighted Average Exercise Price
\$ 7.70 – 11.11	708,663	2.89	\$ 9.41	708,663	\$ 9.41
\$ 13.68 – 16.24	227,800	2.98	\$		