LABARGE INC
Form 10-K
September 07, 2006

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

[X] ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITITES For EXCHANGE ACT OF 1934
For the transition period ______ to ______.

FOR THE FISCAL YEAR ENDED JULY 2, 2006

Commission File Number 1-5761

LaBARGE, INC.

(Exact name of registrant specified in its charter)

DELAWARE
(State or other jurisdiction of incorporation or organization)

73-0574586
(I.R.S. Employer Identification Number)

9900 CLAYTON ROAD, ST. LOUIS, MISSOURI 63124
(Address of principal executive offices)(ZIP Code)

Registrant's telephone number, including area code: (314) 997-0800

Securities registered pursuant to Section 12(b) of the Act:

Title of Class	Name of each exchange on which registered
Common Stock, $.01 par value	American Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:
Series C Junior Participating Preferred Stock Purchase Rights
Title of Class

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

[X] Yes [ ] No [X]

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

[X] Yes [ ] No [X]

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 requirement for the past 90 days. Yes [X] No [ ]

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 Regulation S-K is not contained herein, and will not be contained, to the best of Registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. [X]

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

Large Accelerated Filer [ ] Accelerated Filer [X] Non-Accelerated Filer [ ]

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

[X] Yes [ ] No [X]

As of July 2, 2006, 15,166,991 shares of common stock of the registrant were outstanding; the aggregate market value of the shares of common stock of the registrant held by non-affiliates was approximately $201.3 million, based upon the closing price of $13.27 per share on the American Stock Exchange on June 30, 2006.

DOCUMENTS INCORPORATED BY REFERENCE

Certain portions of the Company's definitive proxy materials relating to the Company's 2007 Annual Meeting of Stockholders to be filed with the Securities and Exchange Commission ("SEC") within 120 days after the end of the Company's fiscal year are incorporated in Part III of this annual report.

LaBarge, Inc.
Form 10-K
For The Year Ended July 2, 2006

PART I

ITEM 1. BUSINESS

General Development of Business and Information about Business Activity

LaBarge, Inc. (“LaBarge” or the “Company”) is a Delaware corporation that manufactures and designs high-performance electronics and interconnect systems on a contract basis for customers in diverse technology-driven markets. The Company’s core competencies are to provide complete electronic systems solutions, including the manufacturing, engineering and design of interconnect systems, circuit card assemblies and high-level assemblies for its customers’ specialized applications.

The Company markets its services to customers desiring an engineering and manufacturing partner capable of developing and providing high-reliability electronic equipment, including products capable of performing in harsh environmental conditions, such as high and low temperature, severe shock and vibration. The Company serves customers in a variety of markets including defense, government systems, aerospace, natural resources, industrial and other commercial markets. The Company’s engineering and manufacturing facilities are located in Arkansas, Missouri, Oklahoma, Texas and Pennsylvania. The Company employs approximately 1,200 people, including approximately 1,010 people (of which 39 are engineers) who provide support for production activities and approximately 190 people who provide administrative support.

On February 17, 2004, the Company acquired substantially all of the assets of Pinnacle Electronics LLC (“Pinnacle” or “the Pittsburgh operation”). The acquired assets supplement the Company’s electronics manufacturing services (“EMS”) business with a leased manufacturing location in metropolitan Pittsburgh, Pennsylvania, substantially enhancing the Company’s commercial/industrial sales mix. Pinnacle’s commercial/industrial market expertise, supported by a strong management team, further diversifies the Company’s historic strength in the government/defense marketplace.

Pinnacle understands the unique characteristics of the commercial/industrial EMS market and has developed competencies and inventory management practices to maximize productivity and profitability. The Pittsburgh operation designs, engineers and manufactures printed circuit card assemblies, cables and harnesses, full “box-build” assemblies and electronic/electromechanical systems for customers in a variety of commercial/industrial markets. The Company believes there will be continued growth in these markets as the trend to outsource non-core-competency manufacturing continues.

The purchase price for Pinnacle was $43.1 million, which included a post-closing working capital adjustment of approximately $2.1 million, and was funded by senior bank debt and cash on hand. In addition, the Company assumed working capital liabilities of approximately $3.7 million, primarily trade accounts payable, and incurred transaction costs of approximately $0.3 million.

The Company’s total net sales were $190.1 million, compared with $182.3 million for fiscal 2005, and $131.5 million for fiscal 2004. The backlog for the Company at July 2, 2006 was $183.9 million, compared with $164.9 million at July 3, 2005, an increase of 11.5%. The growth in backlog is the result of a sales and marketing effort that focuses on matching the Company’s core competencies to the outsourcing needs of targeted large customers in a variety of industries. Approximately $38.9 million and $32.4 million of the backlog at fiscal 2006 year-end and fiscal 2005 year-end, respectively, are scheduled to ship beyond the subsequent 12 months pursuant to the shipment schedules contained in those contracts.

Sales and Marketing

During fiscal 2006, 39.9% of the Company’s revenues were generated from customers in the defense market, 20.5% from natural resources, 17.6% from industrial and 9.9% from the government systems market. The remaining 12.1% of sales came from various customers in the commercial aerospace, medical, telecommunications and other industries. The Company produces electronic equipment for use in a variety of high-technology applications, including military communication and radar systems, industrial automation, military and commercial aircraft, satellites, space launch vehicles, down-hole instrumentation for oil and gas wells, and postal automation equipment. The Company’s broad-based core competencies in electronics design and manufacturing allow it to pursue diverse opportunities with customers in many different markets. The diversification of the Company’s customer base helps protect it from volatility in any one market sector.

With few exceptions, the Company’s sales are made pursuant to fixed-price contracts. Larger, long-term government contracts frequently have provisions for milestone, progress payments or cash advances for purchase of inventory.

The Company seeks to develop strong, long-term relationships with its customers, which will provide the basis for future sales. These close relationships allow the Company to better understand each customer's business needs and identify ways to provide greater value to the customer.

Competition

There is intense competition for all of the Company's targeted customers. While the Company is not aware of another entity that competes in all of its capabilities, there are numerous companies, many larger, which compete in one or more of these capabilities. The Company's customers frequently have the ability to produce internally the products contracted to the Company, but because of cost, capacity, engineering capability or other reasons, outsource production of such products to the Company. The principal bases of competition are service, price, engineering expertise, technical and manufacturing capabilities, quality, reliability, and overall project management capability.

Concentration of Business

Three customers, each with multiple operating units, together accounted for 35% of the Company's consolidated sales in fiscal 2006: Owens-Illinois, Inc., 12%; Northrop Grumman Corporation, 12%; and Schlumberger Ltd., 11%. No other customer accounted for more than 8% of total sales. Sales to the largest 10 customers represented approximately 69% of the Company's total sales in fiscal year 2006 and 72% in fiscal year 2005.

In fiscal years 2006 and 2005, respectively, 49.8% and 48.8% of the Company's net sales derived from sales contracts with original equipment manufacturers ("OEMs") doing business with the U.S. Government or its agencies. Generally, government contracts may be terminated at the convenience of the government. When such contracts are terminated, the Company typically receives payments to cover its direct and indirect costs incurred before termination.

Manufacturing Operations

The Company has organized its engineering and production to provide flexible independent plant locations with specific design and manufacturing capabilities. This approach allows local management at each facility to concentrate the necessary attention on specific customer needs and, at the same time, control all key aspects of the engineering and manufacturing processes.

Generally, there are multiple sources for materials required by the Company for its manufacturing process. However, pursuant to some of its contracts, the Company is limited to a single source for certain electronic components. In most cases, the Company believes that if it were unable to obtain components from the designated source, it would be able to obtain a new source, mutually agreed upon by the parties, without adversely impacting its manufacturing process.

Strategy

The Company's business strategy is to serve as an outsourcing partner to OEMs that do business in diverse markets by providing a package of broad-based manufacturing capabilities and value-added services. This strategy is designed around the Company's core competencies in manufacturing complex electronic assemblies, subsystems and interconnect systems for specialized applications where reliability is critical. The Company's business historically was concentrated in the defense and other government-related markets. In recent years, that focus has broadened to include industrial and commercial customers. This greater market diversity helps protect the Company from downturns in any one market.

Capital Structure

The Company entered into a senior secured loan agreement with a group of banks on February 17, 2004 that was amended on February 10, 2006, increasing the revolving credit facility by $10.0 million. The following is a summary of the agreement:

- A revolving credit facility up to $30.0 million, available for direct borrowings or letters of credit. The facility is based on a borrowing base formula equal to the sum of 85% of eligible receivables and 35% of eligible inventories. As of July 2, 2006, outstanding loans under the revolving credit facility were $19.5 million. Letters of credit outstanding were $1.6 million, and $8.9 million was available at July 2, 2006. This credit facility matures on February 17, 2009.

- A $25.0 million term loan amortized beginning May 2004, at a quarterly rate of $1.0 million, increased to $1.25 million in May 2006 and increasing to $1.5 million in May 2007. Final maturity is February 2009. As of July 2, 2006, the amount outstanding was $15.8 million.

- On April 15, 2004, the Company entered into an Interest Rate Cap Agreement with a bank. This Cap Agreement caps the Company's exposure to increases in LIBOR at 4% for a period of three years on a notional amount beginning at $24.0 million and amortizing on a schedule that matches amortization of the $25.0 million term loan dated February 17, 2004. As a result of this Cap Agreement, for the year-ended period, interest expense was reduced by $72,000.

- Interest on both loans is at a percentage of prime or a stated rate over LIBOR based on certain ratios. For the year ended July 2, 2006, the average rate was approximately 5.89%.

- Both loans are secured by substantially all the assets of the Company other than real estate.

- Covenants and performance criteria consist of Earnings Before Interest, Taxes, Depreciation and Amortization ("EBITDA") in relation to debt, EBITDA in relation to fixed charges and minimum net worth. The Company is in compliance with its borrowing agreement covenants as of July 2, 2006.

Other Long-term Debt:

Mortgage Loan:

The Company has a $6.4 million term loan secured by the Company's headquarters building in St. Louis, Missouri. The loan repayment schedule is based on a 25-year amortization with a final balloon payment due in October 2009. The balance at July 2, 2006 was $5.5 million. Interest is at a percentage of prime or a stated rate over LIBOR based on certain ratios. For the year ended July 2, 2006, the average rate was approximately 4.82%.

Industrial Revenue Bonds:

In July 1998, the Company acquired tax-exempt Industrial Revenue Bond financing in the amount of $1.3 million. The debt is payable over 10 years with an interest rate of 5.28%. This funding was used to expand the Berryville, Arkansas, facility. The outstanding balance at July 2, 2006 was $369,000.

Capital Lease Obligations:

In October 2005, the Company entered into a capital lease agreement to fund the purchase of machinery with a fair market value of $664,000. The lease is for five years with an interest rate of 6.18%. The obligation outstanding at July 2, 2006 was $587,000.

The aggregate maturities of long-term obligations are as follows:

(dollars in thousands)

Fiscal Year	
2007	$ 5,791
2008	6,553
2009	4,937
2010	4,861
2011	51
Thereafter	---
Total	$22,193

Environmental Compliance

Compliance with federal, state and local environmental laws is not expected to materially affect the capital expenditures, earnings or competitive position of the Company.

Financial Information About Foreign and Domestic Operations and Export Sales

No information has been included hereunder because the Company's foreign sales in each of fiscal 2006, fiscal 2005 and fiscal 2004 were less than 10% of the total Company revenue.

Available Information

We make available, free of charge, our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to these reports filed or furnished pursuant to Section 13(a) or 15(d) of the Securities Exchange Act of 1934, as amended, through our website at www.labarge.com as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC.

ITEM 1A. RISK FACTORS

The Company is subject to certain risks and events that, if one or more of them occur, could adversely affect our business, financial condition and results of operations and the trading price of our common stock. You should consider the following risk factors, in addition to other information presented in this report, as well as the other reports and registration statements we file from time to time with the SEC, in evaluating the Company, our business and making an investment in our securities. The risks below are not the only risks that the Company faces. Additional risks not currently known to us or those that we currently deem immaterial may also impair our business.

The Company experiences variable operating results.

The Company's results of operations have varied and may continue to fluctuate significantly from period to period, including on a quarterly basis. Consequently, results of operations in any period should not be considered indicative of the results for any future period, and fluctuations in operating results may also result in fluctuations in the price of the Company's common stock.

The Company's quarterly and annual results may vary significantly depending on numerous factors, many of which are beyond the Company's control. These factors include:

- Changes in sales mix to customers
- Changes in availability and cost of components
- Volume of customer orders relative to capacity
- Market demand and acceptance of our customers' products
- Price erosion within the EMS marketplace
- Capital equipment requirements needed to remain technologically competitive.

The Company's customer base is concentrated.

Significant reduction in sales to any of the Company's major customers or the loss of a major customer could have a material impact on the Company's operations. Although the Company believes its relationships with its large customers are good. There can be no assurance that the Company will retain any or all of its large customers or will be able to form new relationships with customers upon the loss of one or more of its existing customers. This risk may be further complicated by pricing pressures and intense competition prevalent in our industry.

A material portion of the Company's business is dependent on defense contracts with the U.S. Government, which could be adversely affected by cutbacks in government defense spending.

In fiscal 2006 and 2005, respectively, approximately 40% and 45% of the Company's net sales were generated from subcontracts with OEMs on defense contracts with the U.S. Government. The Company's net sales could be negatively impacted as a result of government defense spending cuts, general budgetary constraints, and the complex and competitive government procurement processes. If the Company is unable to maintain this level of government-related sales, or replace government-related contracts with those of comparable non-government customers, the Company's sales and results of operations will be adversely affected.

Some of the Company's contracts involving the government are subject to cancellation at the government's option.

In fiscal 2006 and 2005, respectively, approximately 49.8% and 48.8% of the Company's revenues were derived from subcontracts with OEMs on their contracts with the U.S. government. The government has the right to terminate these contracts without cause for its convenience. While the Company normally recovers its direct and indirect costs, termination of the contract by the government could result in the Company receiving lower than anticipated profits for the Company.

There is variability in the requirements of the Company's customers.

The Company does not generally obtain long-term purchase contracts. The timing of purchase orders placed by the Company's customers is affected by a number of factors, including variation in demand for the customers' products, federal government funding, regulatory changes affecting customer industries, customer attempts to manage their inventory, changes in the customers' manufacturing strategies and customers' technical problems or issues. Many of these factors are outside the control of the Company.

The Company and its customers may be unable to keep current with the industry's technological changes.

The market for the Company's manufacturing services is characterized by rapidly changing technology and continuing product development. The future success of the Company's business will depend in large part upon its and its customers' ability to maintain and enhance its technological capabilities, develop and market manufacturing services which meet changing customer needs, and successfully anticipate or respond to technological changes in manufacturing processes on a cost-effective and timely basis.

Certain of the Company's customers must be in compliance with a new European standard, Restriction of Hazardous Substances in Electrical and Electronic Equipment (RoHS Directive 2002-95-EC) for all products shipped to the European marketplace. The purpose of the directive is to restrict the use of hazardous substances in electrical and electronic equipment and to contribute to the environmentally sound recovery and disposal of electrical and electronic equipment waste. In addition, electronic component manufacturers must produce electronic components that are lead-free. The Company's Pittsburgh operation has implemented lead-free wave solder and reflow systems. The Company relies on numerous third-party suppliers for components used in the Company's production process. Customers' specifications may require the Company to obtain components from a single source or a small number of suppliers. There is no assurance these suppliers will comply with RoHS. The inability to utilize any such suppliers could increase the cost of components and have a material impact on the Company's results of operations.

The Company faces intense industry competition and downward pricing pressures.

The EMS industry is highly fragmented and characterized by intense competition. Some of the Company's competitors have substantially greater manufacturing, purchasing, marketing and financial resources than the Company. Many of the Company's customers have the in-house capability to fulfill their material requirements.

There can be no assurance that competition from existing or potential competitors will not have a material adverse impact on the Company's business, financial condition or results of operations. The introduction of lower priced competitive products, significant price reductions by the Company's competitors or significant pricing pressures from its customers could adversely affect the Company's business, financial condition, and results of operations.

The Company does not have the ability to control, and may not accurately estimate, its costs associated with performing under fixed-price contracts.

Most of the Company's contracts are on a fixed-price basis. In order to realize a profit on these contracts, the Company must, when it bids these contracts, accurately estimate its costs to complete the contracts. Its failure to accurately estimate these costs can result in cost overruns, which result in reduced or lost profits. Estimates of labor costs are most difficult in the case of contracts with new customers. For example, in fiscal 2006, the Company incurred unanticipated labor and other costs in the start-up phases of several contracts with new customers, which had a negative impact on the Company's operating margins.

The availability of raw components may affect the Company's operations.

The Company relies on numerous third-party suppliers for components used in the Company's production process. Certain of these components are available only from single sources or a limited number of suppliers. In addition, a customer's specifications may require the Company to obtain components from a single source or a small number of suppliers. The loss of any such suppliers could have a material impact on the Company's results of operations. The Company could operate at a cost disadvantage compared to competitors who have greater direct buying power from suppliers.

The Company may not be able to replace completed, canceled or reduced contracts with new contracts.

The Company is dependent upon contract awards by its customers. The size and timing of contracts vary from period to period. If the Company is unable to replace completed, canceled or reduced contracts in a timely fashion, revenues and operating results will decline.

The Company is dependent on key personnel.

The Company depends significantly on its executive and plant management. The loss of the services of any of these key employees could have a material impact on the Company's business and results of operations. In addition, despite significant competition, continued growth and expansion of the Company's contract manufacturing business will require that it attract, motivate and retain additional skilled and experienced personnel. The inability to satisfy these requirements could have a negative impact on the Company's ability to remain competitive in the future.

Failure to comply with environmental regulations could subject the Company to liability.

The Company is subject to a variety of environmental regulations relating to the use, storage, discharge and disposal of hazardous chemicals used during its manufacturing process. Any failure by the Company to comply with present or future regulations could subject it to future liabilities or the suspension of production, which could have a material negative impact on the Company's results of operations.

The price of the Company's stock is volatile.

The price of the Company's Common Stock historically has experienced significant volatility due to a number of factors including: fluctuations in the Company's revenue and earnings, the market's changing expectations for the Company's growth, overall equity market conditions, the limited float of the Company's Common Stock and other factors either related or unrelated to the Company's operations. Such fluctuations are expected to continue.

ITEM 1B. UNRESOLVED STAFF COMMENTS

Not applicable.

ITEM 2. PROPERTIES

The Company's principal facilities, which are deemed adequate and suitable for the Company's business, are as follows:

Location	Principal Use	Land (acres)	Buildings (sq. ft.)	Calendar Year of Termination of Lease
Berryville, AR	Manufacturing & Offices	17.5	52,000	Owned
Houston, TX	Manufacturing & Offices	2	33,000	2013
Huntsville, AR	Manufacturing & Offices	6	69,000	2020
Joplin, MO	Manufacturing & Offices	5	60,000	Owned
Joplin, MO	Manufacturing	4	33,000	2008
Joplin, MO	Manufacturing	1	56,600	2011
Pittsburgh, PA	Manufacturing & Offices	5	135,504	2010
Pittsburgh, PA	Manufacturing	1	29,880	2008
St. Louis, MO	Offices	8	65,176	Owned
Tulsa, OK	Manufacturing & Offices	3	55,000	2008
Tulsa, OK	Manufacturing	1	6,425	2008
Tulsa, OK	Offices	.5	3,235	2008

ITEM 3. LEGAL PROCEEDINGS

In March 2004, the Company received notice from the Library of Congress ("LOC") that the LOC was seeking financial restitution in the amount of $1.8 million stemming from the Company's production of audiocassette machines during the period 1992 through 1996. The LOC claimed the machines were defective. The Company disputed the LOC's position.

During the fiscal year ended July 2, 2006, in order to avoid future legal expenses, the Company paid $50,000 to settle all claims related to this issue, without an admission of liability.

In March 2005, the Company entered into a contract with Northrop Grumman Corporation to supply equipment used on mail sorting machines. The equipment to be manufactured and the services to be performed have undergone hundreds of design and component changes. The Company has negotiated a settlement of the claims arising from these changes. During the year ended July 2, 2006, the Company recovered its costs under the claim.

ITEM 4. SUBMISSION OF MATTER TO A VOTE OF SECURITY HOLDERS

There were no items submitted to a vote of the security holders in the quarter ended July 2, 2006.

PART II

ITEM 5. MARKET FOR REGISTRANTS'S COMMON EQUITY AND RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Stock Price and Cash Dividends: LaBarge, Inc.'s Common Stock is listed on the American Stock Exchange, under the trading symbol of "LB." As of September 5, 2006, there were 2,126 holders of record of LaBarge, Inc.'s Common Stock. The following table indicates the quarterly high and low sales prices for the stock for the fiscal years 2006 and 2005, as reported by the American Stock Exchange.

2005-2006	**High**	**Low**
July – September	**$22.00**	**$12.02**
October – December	**15.15**	**12.80**
January – March	**17.76**	**13.90**
April – June	**16.43**	**10.68**

2004-2005	High	Low
July – September	$ 9.00	$ 6.68
October – December	13.50	7.85
January – March	13.75	9.70
April – June	18.40	12.01

The Company has paid no cash dividends on its common stock. The Company currently anticipates that it will retain any future earnings for the development, operation and expansion of its business and for possible acquisitions.

The following table contains certain information as of July 2, 2006 with respect to options granted and outstanding under the Company's three stock option plans, shares available for purchase as of that date under the Company's employee stock purchase plan, weighted average exercise price of outstanding options, warrants and rights, and number of securities remaining available for future issuance under these plans.

Plan category	**Number of securities to be issued upon exercise of outstanding options, warrants and rights**	**Weighted-average exercise price of outstanding options, warrants and rights**	**Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column 1)**
Equity compensation plans approved by security holders	1,771,151	$3.94	4,462
Equity compensation plans not approved by security holders	---	---	---

The following table contains certain information as of July 2, 2006 with respect to restricted stock awards outstanding under the 2004 Long Term Incentive Plan.

Number of securities	**Number of securities remaining available for future issuance under equity compensation plans**

Plan category	to be issued based on outstanding grants	Weighted average price of securities issued	(excluding securities reflected in column 1)
Equity compensation plans approved by security holders	79,693	$13.27	712,556
Equity compensation plans not approved by security holders	---	---	---

In August 2005, the Company's Board of Directors authorized the Company to repurchase up to 1 million shares of its Common Stock. In the quarter ended July 2, 2006, the Company repurchased 54,600 shares of its Common Stock. The following table discloses certain information relating to these repurchases.

ISSUER PURCHASES OF EQUITY SECURITIES

Period	Total Number of Shares (or Units) Purchased	Average Price Paid per Share (or Unit)	Total Number of Shares (or Units) Purchased as Part of Publicly Announced Plans or Programs (1)	Maximum Number (or Approximate Dollar Value) of Shares (or Units) that May Yet Be Purchased Under the Plans or Programs
April 3 - April 30	---	---	---	988,700
May 1 - May 28 &	13,700	$13.40	13,700	975,000