

UFP TECHNOLOGIES INC
Form 10-Q
August 08, 2014
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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, DC 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 JUNE 30, 2014

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: 001-12648

UFP Technologies, Inc.

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(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

04-2314970

(IRS Employer Identification No.)

172 East Main Street, Georgetown, Massachusetts 01833, USA

(Address of principal executive offices) (Zip Code)

(978) 352-2200

(Registrant's telephone number, including area code)

(Former name, former address, and former fiscal year, if changed since last report)

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 has submitted electronically and posted on its corporate website, 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 x; No o

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 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

Smaller reporting company

[Do not check if a 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 o; No x

7,054,173 shares of registrant's Common Stock, \$0.01 par value, were outstanding as of August 1, 2014.

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UFP Technologies, Inc.

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Table of Contents**PART I: FINANCIAL INFORMATION****ITEM 1: FINANCIAL STATEMENTS****UFP Technologies, Inc.****Condensed Consolidated Balance Sheets**

(In thousands, except share data)

	June 30, 2014 (Unaudited)	December 31, 2013
Assets		
Current assets:		
Cash and cash equivalents	\$ 31,960	\$ 37,303
Receivables, less allowance for doubtful accounts of \$473 at June 30, 2014 and \$512 at December 31, 2013	17,622	17,032
Inventories	13,429	11,048
Prepaid expenses	1,681	690
Refundable income taxes	1,625	1,537
Deferred income taxes	1,256	1,222
Total current assets	67,573	68,832
Property, plant, and equipment	68,546	64,574
Less accumulated depreciation and amortization	(40,755)	(39,067)
Net property, plant, and equipment	27,791	25,507
Goodwill	7,322	7,322
Intangible assets, net	1,114	1,346
Other assets	5,084	2,013
Total assets	\$ 108,884	\$ 105,020
Liabilities and Stockholders Equity		
Current liabilities:		
Accounts payable	\$ 4,161	\$ 3,081
Accrued expenses	6,834	8,265
Current installments of long-term debt	985	976
Total current liabilities	11,980	12,322
Long-term debt, excluding current installments	2,372	2,867
Deferred income taxes	2,245	2,436
Retirement and other liabilities	1,589	1,805
Total liabilities	18,186	19,430
Commitments and contingencies		
Stockholders equity:		
Preferred stock, \$.01 par value. Authorized 1,000,000 shares; zero shares issued or outstanding		
Common stock, \$.01 par value. Authorized 20,000,000 shares; issued and outstanding 7,054,173 at June 30, 2014 and 6,900,683 at December 31, 2013	71	69
Additional paid-in capital	21,475	20,291
Retained earnings	69,152	65,230
Total stockholders equity	90,698	85,590
Total liabilities and stockholders equity	\$ 108,884	\$ 105,020

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

Table of Contents**UFP Technologies, Inc.****Condensed Consolidated Statements of Income**

(In thousands, except share data)

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2014	2013	2014	2013
Net sales	\$ 34,025	\$ 35,832	\$ 68,634	\$ 69,529
Cost of sales	24,549	25,113	50,050	49,908
Gross profit	9,476	10,719	18,584	19,621
Selling, general & administrative expenses	6,466	6,075	12,290	12,021
Restructuring costs	234		324	
(Gain) loss on sale of fixed assets	(12)	11	(12)	11
Operating income	2,788	4,633	5,982	7,589
Interest expense, net	(27)	(45)	(48)	(85)
Other income, net	100		100	
Income before income tax expense	2,861	4,588	6,034	7,504
Income tax expense	1,001	1,606	2,112	2,492
Net income	\$ 1,860	\$ 2,982	\$ 3,922	\$ 5,012
<i>Net income per share:</i>				
Basic	\$ 0.27	\$ 0.44	\$ 0.56	\$ 0.74
Diluted	\$ 0.26	\$ 0.42	\$ 0.55	\$ 0.71
<i>Weighted average common shares outstanding:</i>				
Basic	7,025	6,798	6,999	6,783
Diluted	7,168	7,090	7,160	7,089

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

Table of Contents**UFP Technologies, Inc.****Condensed Consolidated Statements of Cash Flows**

(In thousands)

(Unaudited)

Cash flows from operating activities:			
Net income	\$	3,922	\$ 5,012
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization		2,247	1,977
(Gain) loss on sale of fixed assets		(12)	11
Share-based compensation		730	507
Excess tax benefit on share-based compensation		(834)	(8)
Deferred income taxes		(225)	(7)
Changes in operating assets and liabilities:			
Receivables, net		(590)	(826)
Inventories		(2,381)	(1,196)
Prepaid expenses		(991)	(540)
Refundable income taxes		746	1,714
Other assets		(103)	(106)
Accounts payable		1,080	(108)
Accrued taxes and other expenses		(1,431)	(1,559)
Retirement and other liabilities		(216)	203
Net cash provided by operating activities		1,942	5,074
Cash flows from investing activities:			
Additions to property, plant, and equipment		(4,309)	(3,545)
Escrow deposit for Texas building purchase (See Note 12)		(2,968)	
Holdback payment related to the acquisition of Packaging Alternatives Corporation			(200)
Proceeds from sale of fixed assets		22	5
Net cash used in investing activities		(7,255)	(3,740)
Cash flows from financing activities:			
Proceeds from the issuance of long-term debt			580
Principal repayments of long-term debt		(486)	(770)
Proceeds from exercise of stock options, net of attestation		323	65
Excess tax benefit on share-based compensation		834	8
Payment of statutory withholdings for stock options exercised and restricted stock units vested		(701)	(426)
Net cash used in financing activities		(30)	(543)
Net (decrease) increase in cash and cash equivalents		(5,343)	791
Cash and cash equivalents at beginning of period		37,303	33,480
Cash and cash equivalents at end of period	\$	31,960	\$ 34,271

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

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Notes to Interim Condensed Consolidated Financial Statements

(1) Basis of Presentation

The interim condensed consolidated financial statements of UFP Technologies, Inc. (the Company) presented herein, have been prepared pursuant to the rules of the Securities and Exchange Commission for quarterly reports on Form 10-Q and do not include all the information and note disclosures required by accounting principles generally accepted in the United States of America. These statements should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2013, included in the Company's 2013 Annual Report on Form 10-K as filed with the Securities and Exchange Commission.

The condensed consolidated balance sheet as of June 30, 2014, the condensed consolidated statements of income for the three- and six-month periods ended June 30, 2014, and 2013, and the condensed consolidated statements of cash flows for the six-month periods ended June 30, 2014, and 2013 are unaudited but, in the opinion of management, include all adjustments (consisting of normal, recurring adjustments) necessary for a fair presentation of results for these interim periods.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period.

The results of operations for the three- and six-month periods ended June 30, 2014, are not necessarily indicative of the results to be expected for the entire fiscal year ending December 31, 2014.

(2) Supplemental Cash Flow Information

Cash paid for interest and income taxes is as follows (in thousands):

	Six Months Ended June 30,			
	2014		2013	
Interest	\$	47	\$	86
Income taxes, net of refunds	\$	1,589	\$	645

During the six-month periods ended June 30, 2014, and 2013, the Company permitted the exercise of stock options with exercise proceeds paid with the Company's stock (cashless exercises) totaling approximately \$352,000 and \$0, respectively.

(3) Fair Value Accounting

The Company has financial instruments, such as accounts receivable, accounts payable, and accrued expenses, which are stated at carrying amounts that approximate fair value because of the short maturity of those instruments. The carrying amount of the Company's long-term debt approximates fair value as the interest rate on the debt approximates the estimated borrowing rate currently available to the Company.

(4) Share-Based Compensation

Share-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as an expense over the requisite service period (generally the vesting period of the equity grant).

The Company issues share-based payments through several plans that are described in detail in the notes to the consolidated financial statements for the year ended December 31, 2013. The compensation cost charged against income for those plans is included in selling, general & administrative expenses as follows (in thousands):

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	Three Months Ended June 30,			Six Months Ended June 30,		
	2014	2013	2013	2014	2013	2013
Total share-based compensation expense	\$ 465	\$ 328	\$ 328	\$ 730	\$ 507	\$ 507

Share-based compensation for the three-month periods ended June 30, 2014 and 2013 includes approximately \$122,000 and \$60,000, respectively, representing the fair value of the Company's common stock granted during the quarter to the Board of Directors. Share-based compensation for the six-month periods ended June 30, 2014 and 2013 includes approximately \$127,000 and \$60,000, respectively, representing the fair value of the Company's common stock granted during the period to the Board of Directors.

The total income tax benefit recognized in the condensed consolidated statements of income for share-based compensation arrangements was approximately \$145,000 and \$106,000 for the three-month periods ended June 30, 2014, and 2013, respectively, and \$215,000 and \$157,000 for the six-month periods ended June 30, 2014, and 2013, respectively.

The following is a summary of stock option activity under all plans for the six-month period ended June 30, 2014:

	Shares Under Options	Weighted Average Exercise Price (per share)	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2013	467,500	\$ 9.00		
Granted	30,193	25.05		
Exercised	(159,336)	4.23		
Cancelled or expired				
Outstanding at June 30, 2014	338,357	\$ 12.67	4.31	\$ 3,892
Exercisable at June 30, 2014	249,608	\$ 9.95	4.45	\$ 3,545
Vested and expected to vest at June 30, 2014	338,357	\$ 12.67	4.31	\$ 3,892

On March 12, 2014, the Company granted one of its directors options to purchase 577 shares of its common stock at that day's closing price of \$25.48. On June 11, 2014, the Company granted options to certain employees and directors for the purchase of 15,000 shares and 14,616 shares, respectively, of common stock at that day's closing price of \$25.04. The compensation expense related to these grants was determined as the fair value of the options using the Black Scholes option pricing model based on the following assumptions:

Expected volatility	32.8% to 37.9%
Expected dividends	None
Risk free interest rate	0.7% to 0.8%
Expected term	3.8 to 5.0 years

The stock volatility for each grant is determined based on a review of the experience of the weighted average of historical daily price changes of the Company's common stock over the expected option term, and the risk-free rate is based on the U.S. Treasury yield curve in effect at the time of grant for periods corresponding with the expected life of the option. The weighted average grant date fair value of options granted during the six-month period ended June 30, 2014 was \$7.47.

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During the six-month periods ended June 30, 2014, and 2013, the total intrinsic value of all options exercised (i.e., the difference between the market price on the exercise date and the price paid by the employees to exercise the options) was approximately \$3.4 million and \$155,000, respectively, and the total amount of consideration received by the Company from the exercised options was approximately \$675,000 and \$65,000,

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respectively. At its discretion, the Company allows option holders to surrender previously owned common stock in lieu of paying the exercise price and withholding taxes. During the six-months ended June 30, 2014, 31,310 shares (14,077 for options and 17,233 for taxes) were surrendered at an average market price of \$25.47.

During the three-month periods ended June 30, 2014, and 2013, the Company recognized compensation expenses related to stock options granted to directors and employees of approximately \$172,000 and \$100,000, respectively. During the six-month periods ended June 30, 2014, and 2013, the Company recognized compensation expenses related to stock options granted to directors and employees of approximately \$267,000 and \$125,000, respectively.

On February 18, 2014, the Company's Compensation Committee approved the award of \$400,000, payable in shares of common stock to the Company's Chairman, Chief Executive Officer, and President under the 2003 Incentive Plan. The shares will be issued on or before December 31, 2014. The Company recorded compensation expense associated with the award of \$100,000 and \$200,000, respectively, during both the three- and six-month periods ended June 30, 2014 and 2013.

The following table summarizes information about Restricted Stock Units (RSUs) activity during the six-month period ended June 30, 2014:

	Restricted Stock Units	Weighted Average Award Date Fair Value
Unvested at December 31, 2013	50,900	\$ 11.94
Awarded	22,338	25.94
Shares vested	(30,253)	10.11
Forfeited / cancelled		
Unvested at June 30, 2014	42,985	\$ 17.70

During the three- and six-month periods ended June 30, 2014, the Company recorded compensation expense related to RSUs of approximately \$70,000 and \$136,000, respectively. The Company recorded compensation expense of approximately \$68,000 and \$122,000, respectively, for the same periods of 2013.

At the Company's discretion, RSU holders are given the option to net-share settle to cover the required minimum withholding tax, and the remaining amount is converted into the equivalent number of common shares. During the six-month periods ended June 30, 2014 and 2013, 9,878 and 22,089 shares were surrendered at an average market price of \$25.88 and \$19.29, respectively.

At June 30, 2014, the company had approximately \$1.0 million of unrecognized compensation expense which is expected to be recognized over a period of 4.0 years.

(5) **Inventories**

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Inventories are stated at the lower of cost (first-in, first-out) or market, and consist of the following at the stated dates (in thousands):

	June 30, 2014		December 31, 2013	
Raw materials	\$	8,296	\$	6,627
Work in process		1,248		1,056
Finished goods		3,885		3,365
Total inventory	\$	13,429	\$	11,048

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On March 18, 2009, the Company declared a dividend of one preferred share purchase right (a Right) for each outstanding share of common stock, par value \$0.01 per share, to the stockholders of record on March 20, 2009. Each Right entitles the registered holder to purchase from the Company one one-thousandth of a share of Series A Junior Participating Preferred Stock, par value \$0.01 per share (the Preferred Share) of the Company, at a price of \$25 per one one-thousandth of a Preferred Share subject to adjustment and the terms of the Rights Agreement. The Rights expire on March 19, 2019.

(7) Income Per Share

Basic income per share is based on the weighted average number of shares of common stock outstanding. Diluted income per share is based upon the weighted average number of common shares outstanding and dilutive common stock equivalent shares outstanding during each period.

The weighted average number of shares used to compute basic and diluted net income per share consisted of the following (in thousands):

	Three Months Ended		Six Months Ended	
	2014	2013	2014	2013
Weighted average common shares outstanding, basic	7,025	6,798	6,999	6,783
Weighted average common equivalent shares due to stock options and RSUs	143	292	161	306
Weighted average common shares outstanding, diluted	7,168	7,090	7,160	7,089

The computation of diluted earnings per share excludes the effect of the potential exercise of stock awards, including stock options, when the average market price of the common stock is lower than the exercise price of the related options during the period. These outstanding stock awards are not included in the computation of diluted income per share because the effect would have been antidilutive. For both the three- and six-month periods ended June 30, 2014, the number of stock awards excluded from the computation of diluted earnings per share was 30,193. For both the three- and six-month periods ended June 30, 2013, the number of stock awards excluded from the computation of diluted earnings per share was 77,362.

(8) Segment Reporting

The Company is organized based on the nature of the products and services that it offers. Under this structure, the Company produces products within two distinct segments: Component Products and Packaging. Within the Component Products segment, the Company primarily uses cross-linked polyethylene foam to provide customers in the medical, aerospace and defense, automotive, and packaging markets with engineered products for numerous purposes. Within the Packaging segment, the Company primarily uses polyethylene and polyurethane foams, sheet

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plastics, and pulp fiber to provide customers with cushion packaging for their products.

The accounting policies of the segments are the same as those described in Note 1 to the consolidated financial statements contained in the Company's annual report on Form 10-K for the year ended December 31, 2013, as filed with the Securities and Exchange Commission. The Company evaluates the performance of its operating segments based on operating income.

Inter-segment transactions are uncommon and not material. Therefore, they have not been reflected separately in the financial table below. Revenues from customers outside of the United States are not material. No customer comprised more than 10% of the Company's consolidated revenues for the three-month period ended June 30, 2014. All of the Company's assets are located in the United States. Unallocated assets consist of the Company's cash balance and unallocated operating income consists of restructuring costs. Financial statement information by reportable segment is as follows (in thousands):

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	Three Months Ended June 30, 2014			Total UFPT \$	Three Months Ended June 30, 2013			Total UFPT \$
	Component Products \$	Packaging \$	Unallocated \$		Component Products \$	Packaging \$	Unallocated \$	
Net sales	23,888	10,137		34,025	24,827	11,005		35,832
Operating income	2,429	593	(234)	2,788	3,217	1,416		4,633
Depreciation / amortization	481	635		1,116	463	540		1,003
Capital expenditures	2,022	909		2,931	196	2,097		2,293

	Six Months Ended June 30, 2014			Total UFPT \$	Six Months Ended June 30, 2013			Total UFPT \$
	Component Products \$	Packaging \$	Unallocated \$		Component Products \$	Packaging \$	Unallocated \$	
Net sales	47,499	21,135		68,634	47,659	21,870		69,529
Operating income	4,872	1,434	(324)	5,982	5,958	1,631		7,589
Depreciation / amortization	979	1,268		2,247	908	1,069		1,977
Capital expenditures	2,395	1,914		4,309	948	2,597		3,545
Total assets	32,582	44,342	31,960	108,884	34,707	32,946	34,272	101,925

(9) **Other Intangible Assets**

The carrying values of the company's definite lived intangible assets as of June 30, 2014, and December 31, 2013, are as follows (in thousands):

	Patents 14 years	Non- Compete 5 years	Customer List 5 years	Total
Estimated useful life				
Gross amount at June 30, 2014	\$ 429	\$ 512	\$ 2,046	\$ 2,987
Accumulated amortization at June 30, 2014	(429)	(294)	(1,150)	(1,873)
Net balance at June 30, 2014	\$	\$ 218	\$ 896	\$ 1,114
Gross amount at December 31, 2013	\$ 429	\$ 512	\$ 2,046	\$ 2,987
Accumulated amortization at December 31, 2013	(429)	(249)	(963)	(1,641)
Net balance at December 31, 2013	\$	\$ 263	\$ 1,083	\$ 1,346

Amortization expense related to intangible assets was approximately \$113,000 and \$105,000 for the three-month periods ended June 30, 2014, and 2013, respectively, and \$232,000 and \$239,000 for the six-month periods ended June 30, 2014, and 2013. The estimated remaining amortization expense as of June 30, 2014 is as follows (in thousands):

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Remainder of:	
2015	318
2017	318

(10) Income Taxes

The income tax expense included in the accompanying unaudited consolidated statements of income principally relates to the Company's proportionate share of the pre-tax income of its majority-owned subsidiaries. The determination of income tax expense for interim reporting purposes is based upon the estimated effective tax rate for the year, adjusted for the impact of any discrete items which are accounted for in the period in which they occur.

The Company recorded a tax expense of approximately 35.0% of income before income tax expense for the three-month periods ended June 30, 2014 and 2013, respectively. The Company recorded a tax expense of approximately 35.0% of income before income tax expense for the six-month period ended June 30, 2014, compared to a tax expense of approximately 33.2% for the comparable six-month period in 2013. The increase in the effective tax rate was a result of a retroactive application for a 2012 research and development credit which was recorded as a discrete event in the first quarter of 2013. Excluding this discrete event, the effective tax rate for the six-months ended June 30, 2013 was also approximately 35.0%.

(11) Plant Consolidation

On January 7, 2014, the Company committed to move forward with a plan to cease operations at its Glendale Heights, Illinois plant and consolidate operations into its Grand Rapids, Michigan, facility. The Company's decision was in response to a pending significant increase in lease cost, declining sales at the Illinois facility, and significant anticipated savings as a result of the consolidation.

The Company expects to incur approximately \$1,150,000 in one-time expenses in connection with the consolidation, and to invest approximately \$300,000 in building improvements in Grand Rapids. Included in the \$1,150,000 amount above are approximately \$350,000 of expenses the Company expects to incur relating to employee severance payments, approximately \$550,000 in moving expenses and expenses associated with vacating the Glendale Heights building, and approximately \$250,000 in expenses in moving equipment within the Grand Rapids location. Total cash charges are estimated at \$1,450,000. The Company expects annual cost savings of approximately \$750,000 as a result of the plant consolidation.

The Company has recorded the following restructuring costs associated with the plant consolidation for the three and six-month periods ended June 30, 2014 (in thousands):

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Restructuring Costs	Three Months Ended June 30, 2014		Six Months Ended June 30, 2014	
Employee severance payments	\$	14	\$	25
Relocation costs		106		115
Workforce training costs		65		113
Grand Rapids plant infrastructure costs		49		71
Total restructuring costs	\$	234	\$	324

The Company also incurred approximately \$131,000 for the three- and six-month periods ended June 30, 2014, in related capital improvements at its Grand Rapids facility.

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(12) Subsequent Events

Plant Consolidation

On July 16, 2014, the Company committed to move forward with a plan to cease operations at its Costa Mesa, California plant and consolidate operations into its Rancho Dominguez, California facility and other UFP facilities. The Company's decision was in response to the December 31, 2014 expiration of the lease on the Costa Mesa facility as well as the close proximity of the two properties. The Company expects the activities related to this consolidation to be completed on or before December 31, 2014.

The Company expects to incur approximately \$535,000 in one-time expenses in connection with the consolidation. Included in the \$535,000 amount above are approximately \$50,000 of expenses the Company expects to incur relating to employee severance payments, approximately \$465,000 in moving expenses and expenses associated with vacating the Costa Mesa property and approximately \$20,000 in expenses in moving equipment within the Rancho Dominguez location. The Company does not expect to incur any lease separation costs as the completion of the move is expected to coincide with the expiration of the Costa Mesa lease. Total cash charges are estimated at \$535,000. The Company expects annual cost savings of approximately \$550,000 as a result of the plant consolidation.

Building Purchase

On July 1, 2014, the Company completed the purchase of a new facility in El Paso, Texas, for approximately \$3.0 million. The Company plans for the new facility to house the Company's current Texas foam and medical packaging business and to provide capacity to expand its molded fiber operations. The expansion will include two additional manufacturing lines that are expected to be operational by the first quarter of 2015.

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ITEM 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-looking Statements

This report contains certain statements that are forward-looking statements as that term is defined under the Private Securities Litigation Reform Act of 1995 and releases issued by the Securities and Exchange Commission. The words believe, expect, anticipate, intend, plan, estimate, and other expressions, which are predictions of or indicate future events and trends and that do not relate to historical matters, identify forward-looking statements. Examples of forward-looking statements included in this report include, without limitation, statements regarding the anticipated financial performance and/or future business prospects of the Company, anticipated trends in the different markets in which the Company competes, expectations regarding the Company's results of operations, financial condition and the sufficiency of the Company's capital resources, statements regarding the Company's capital expenditure plans and expansion of our business and anticipated advantages associated therewith, including the development of and investments in its molded fiber product line, expectations regarding the manufacturing capacity and efficiencies of the Company's production equipment, anticipated advantages relating to the Company's decisions to consolidate its Midwest and California facilities and the expected costs, savings and efficiencies associated therewith, expected methods of growth for the Company, expectations regarding the Company's acquisition strategy, any indication that the Company may be able to sustain or increase its sales and earnings or sales and earnings growth rates and statements regarding the overall economy.

Forward-looking statements involve known and unknown risks, uncertainties and other factors, which may cause the actual results, performance, or achievements of the Company to differ materially from anticipated future results, performance, or achievements expressed or implied by such forward-looking statements. Examples of these risks, uncertainties, and other factors include, without limitation, the following: economic conditions that affect sales of the products of the Company's customers, risks associated with the identification of suitable acquisition candidates and the successful, efficient execution and integration of such acquisitions, the implementation of new production equipment in a timely, cost-efficient manner, risks that any benefits from such new equipment may be delayed or not fully realized, or that the Company may be unable to fully utilize its production capacity, actions by the Company's competitors, and the ability of the Company to respond to such actions, the ability of the Company to obtain new customers, the ability of the Company to offset lost revenues, evolving customer requirements, difficulties associated with the roll-out of new products, decisions by customers to cancel or defer orders for the Company's products that previously had been accepted, risks and uncertainties associated with plant closures and expected efficiencies from consolidating manufacturing, the costs of compliance with the requirements of Sarbanes-Oxley, and general economic and industry conditions and other factors. In addition to the foregoing, the Company's actual future results could differ materially from those projected in the forward-looking statements as a result of the risk factors set forth elsewhere in this report and changes in general economic conditions, interest rates and the assumptions used in making such forward-looking statements. All of the forward-looking statements are qualified in their entirety by reference to the risk factors and other disclaimers described in the Company's filings with the Securities and Exchange Commission, in particular its most recent Annual Report on Form 10-K. The Company undertakes no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise.

Unless the context requires otherwise, the terms *we*, *us*, *our*, or *the Company* refer to UFP Technologies, Inc. and its consolidated subsidiaries.

Overview

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Using foams, plastics, composites, and natural fiber materials, UFP Technologies designs and manufactures a vast range of solutions primarily for the medical, aerospace and defense, automotive, and packaging markets.

The Company realized a 1.3% decrease in year-to-date sales through June 30, 2014, compared to the same period in 2013, largely due to a 19% reduction in sales to the aerospace and defense market due to continued cuts in government spending. This decline in sales, combined with higher overhead costs and approximately \$324,000 in restructuring costs resulted in a 21.2% decrease in operating income for the six-month period ended June 30, 2014. The Company anticipates improved sales to the aerospace and defense market in the second half of 2014 based on customer forecasts but also expects to incur additional restructuring charges associated with the previously announced plant consolidations in the Midwest and in California.

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The Company's current strategy includes organic growth and growth through strategic acquisitions.

Results of Operations

Sales

Sales for the three-month period ended June 30, 2014, decreased approximately 5.0% to \$34.0 million from sales of \$35.8 million for the same period in 2013. Sales for the six-month period ended June 30, 2014, decreased approximately 1.3% to \$68.6 million from sales of \$69.5 million for the same period in 2013. The decrease in sales for the three-month period ended June 30, 2014, is primarily due to a 25.1% sales decline in the aerospace and defense market (both segments) due to continued cuts in government spending and a 16.2% decline in sales to the automotive market (Component Products segment) due largely to customer plant shutdowns. The decrease in sales for the six-month period ended June 30, 2014, is primarily due to a 19.2% sales decline in the aerospace and defense market (both segments) due to continued cuts in government spending partially offset by a 9.1% increase in sales of molded fiber packaging (Packaging segment) due to continued demand for environmentally friendly packaging and the Company's recent addition of production capacity.

Gross Profit

Gross profit as a percentage of sales (gross margin) decreased to 27.9% for the three-month period ended June 30, 2014, from 29.9% for the same period in 2013. This decrease is primarily due to the impact of the sales decrease discussed above measured against fixed overhead, higher depreciation costs and increased employee health care costs. As a percentage of sales, material, and labor collectively declined 0.2% while overhead increased 2.3% (both segments).

Gross profit as a percentage of sales decreased to 27.1% for the six-month period ended June 30, 2014, from 28.2% in the same period of 2013. This decrease is primarily due to the impact of the sales decrease discussed above measured against fixed overhead, higher depreciation costs and increased employee health care costs. As a percentage of sales, material, and labor collectively declined 0.4% while overhead increased 1.5% (both segments).

Selling, General and Administrative Expenses

Selling, general, and administrative expenses (SG&A) increased approximately 6.4% to \$6.5 million for the three-month period ended June 30, 2014, from \$6.1 million for the same period in 2013. SG&A increased approximately 2.2% to \$12.3 for the six-month period ended June 30, 2014, from \$12.0 million in the same period in 2013. The increase in SG&A for the three-month period ended June 30, 2014 is primarily due to higher depreciation costs of approximately \$55,000 largely associated with the Company's new Enterprise Resource Planning (ERP) software system, increased bad debt expense of approximately \$90,000 largely due to one large account write-off and increased director compensation of approximately \$125,000. The slight increase for the six-month period ended June 30, 2014 is primarily due to higher depreciation costs of approximately \$100,000 largely associated with the Company's new ERP software system, increased compensation and benefits of approximately \$330,000 and increased director compensation of approximately \$135,000, partially offset by a reduction of approximately

\$250,000 in professional fees.

Restructuring Costs

On January 7, 2014, the Company committed to move forward with a plan to cease operations at its Glendale Heights, Illinois, plant and consolidate operations into its Grand Rapids, Michigan, facility. The Company's decision was in response to a pending significant increase in lease cost, declining sales at the Illinois facility, and significant anticipated savings as a result of the consolidation.

The Company expects to incur approximately \$1,150,000 in one-time expenses in connection with the consolidation, and to invest approximately \$300,000 in building improvements in Grand Rapids. Included in the \$1,150,000 amount above are approximately \$350,000 of expenses the Company expects to incur relating to employee severance payments, approximately \$550,000 in moving expenses and expenses associated with vacating the Glendale Heights building, and approximately \$250,000 in expenses in moving equipment within the Grand Rapids location. Total cash charges are estimated at \$1,450,000. The Company expects annual cost savings of approximately \$750,000 as a result of the plant consolidation.

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The Company has recorded the following restructuring costs associated with the plant consolidation for the three and six-month periods ended June 30, 2014 (in thousands):

Restructuring Costs	Three Months Ended June 30, 2014		Six Months Ended June 30, 2014	
Employee severance payments	\$	14	\$	25
Relocation costs		106		115
Workforce training costs		65		113
Grand Rapids plant infrastructure costs		49		71
Total restructuring costs	\$	234	\$	324

The Company also incurred approximately \$131,000 for the three and six month periods ended June 30, 2014, in related capital improvements at its Grand Rapids facility.

Interest Expense

The Company had net interest expense of approximately \$27,000 and \$48,000 for the three- and six-month periods ended June 30, 2014, respectively, compared to net interest expense of approximately \$45,000 and \$85,000, respectively, in the same periods of 2013. The decrease in interest expense in both periods, is primarily due to a lower average debt balance as a result of the Company's repayment of term loans in conjunction with the execution of a new revolving credit facility in the fourth quarter of 2013.

Income Taxes

The Company's effective tax rate was approximately 35.0% for the three-month periods ended June 30, 2014 and 2013, respectively. The Company's effective tax rate was approximately 35.0% for the six-month period ended June 30, 2014, compared to an effective tax rate of approximately 33.2% for the comparable six-month period in 2013. The increase in the effective tax rate in the six-month period ended June 30, 2014 was a result of a retroactive application for a 2012 research and development credit which was recorded as a discrete event in the first quarter of 2013. Excluding this discrete event, the effective tax rate for the six months ended June 30, 2013 was also approximately 35.0%.

Liquidity and Capital Resources

The Company generally funds its operating expenses, capital requirements, and growth plan through internally generated cash and bank credit facilities.

Cash Flows

Net cash provided by operations for the six-month period ended June 30, 2014, was approximately \$1.9 million, and was primarily a result of net income generated of approximately \$3.9 million, an increase in refundable income taxes of approximately \$0.7 million and an increase in accounts payable of approximately \$1.1 million due to the timing of vendor payments in the ordinary course of business. These cash inflows were partially offset by an increase in inventory of approximately \$2.4 million due to the timing of raw materials purchases and customer shipments, an increase in prepaid expenses of approximately \$1.0 million primarily due to the prepayment of insurance premiums and a decrease in accrued expenses of approximately \$1.4 million due to payments for 2013 year-end bonuses, annual profit sharing contributions and sales commissions.

Net cash used in investing activities during the six-month period ended June 30, 2014 was approximately \$7.3 million and was primarily the result of additions of manufacturing machinery and equipment and an escrow deposit made with respect to the Company's recent purchase of a new manufacturing facility in Texas.

Net cash used in financing activities was approximately \$30,000 in the six-month period ended June 30, 2014, representing cash used to service term debt of approximately \$480,000 and to pay statutory withholding for stock options exercised and restricted stock units vested of approximately \$700,000, partially offset by excess tax benefits on share-based compensation of approximately \$830,000 and net proceeds received upon stock option exercises of approximately \$320,000.

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Outstanding and Available Debt

The Company maintains an unsecured \$40 million revolving credit facility with Bank of America, N.A. The credit facility calls for interest of LIBOR plus a margin that ranges from 1.0% to 1.5% or, at the discretion of the Company, the bank's prime rate less a margin that ranges from 0.25% to zero. In both cases the applicable margin is dependent upon Company performance. Under the credit facility, the Company is subject to a minimum fixed-charge coverage financial covenant as well as a maximum total funded debt to EBITDA financial covenant. The Company's \$40 million credit facility matures on November 30, 2018.

As of June 30, 2014, the Company had no borrowings outstanding under the credit facility and the Company was in compliance with all covenants under the credit facility.

In 2012, the Company financed the purchase of two molded fiber machines through five-year term loans that mature in September 2017. The annual interest rate is fixed at 1.83% and the loans are secured by the related molded fiber machines. As of June 30, 2014, the outstanding balance of the term loan facility was approximately \$3.4 million.

Future Liquidity

The Company requires cash to pay its operating expenses, purchase capital equipment, and to service its contractual obligations. The Company's principal sources of funds are its operations and its revolving credit facility. The Company generated cash of approximately \$1.9 million in operations during the six-month period ended June 30, 2014, and cannot guarantee that its operations will generate cash in future periods. The Company's longer-term liquidity is contingent upon future operating performance.

Throughout fiscal 2014, the Company plans to continue to add capacity to enhance operating efficiencies in its manufacturing plants. The Company may consider additional acquisitions of companies, technologies, or products that are complementary to its business. The Company believes that its existing resources, including its revolving credit facility, together with cash expected to be generated from operations and funds expected to be available to it through any necessary equipment financings and additional bank borrowings, will be sufficient to fund its cash flow requirements, including capital asset acquisitions, through the next twelve months.

Commitments and Contractual Obligations

There have been no material changes outside the ordinary course of business to our contractual obligations and commitments, as disclosed in our Annual Report on Form 10-K for the year ended December 31, 2013.

Off-Balance-Sheet Arrangements

The Company had no off-balance-sheet arrangements during the six-month period ended June 30, 2014, other than operating leases.

ITEM 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no material changes in our market risks as previously disclosed in Item 7A of our Annual Report on Form 10-K for the year ended December 31, 2013.

ITEM 4: CONTROLS AND PROCEDURES

As of the end of the period covered by this report (the Evaluation Date), the Company's management, under the supervision and with the participation of the Company's Chief Executive Officer and Chief Financial Officer, performed an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in SEC Rule 13a-15(e) or 15d-15(e)). Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of the Evaluation Date, the Company's disclosure controls and procedures were effective to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934, as amended, is (i) recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and (ii)

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accumulated and communicated to the Company's management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

There has been no change in the Company's internal control over financial reporting during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II: OTHER INFORMATION

ITEM 1A: RISK FACTORS

There have been no material changes from the risk factors previously disclosed in Part 1 - Item 1A of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2013.

ITEM 6: EXHIBITS

Exhibit No.	Description
31.1	Rule 13a-14(a)/15d-14(a) Certification of the Chief Executive Officer.*
31.2	Rule 13a-14(a)/15d-14(a) Certification of the Chief Financial Officer.*
32.1	Certifications pursuant to 18 U.S.C., Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.**
101.INS	XBRL Instance Document.*
101.SCH	XBRL Taxonomy Extension Schema Document.*
101.CAL	XBRL Taxonomy Calculation Linkbase Document.*
101.LAB	XBRL Taxonomy Label Linkbase Document.*
101.PRE	XBRL Taxonomy Presentation Linkbase Document.*
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document.*

* Filed herewith.

** Furnished herewith.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

UFP TECHNOLOGIES, INC.

Date: August 8, 2014

By: /s/ R. Jeffrey Bailly
R. Jeffrey Bailly
Chairman, Chief Executive Officer, President, and Director
(Principal Executive Officer)

Date: August 8, 2014

By: /s/ Ronald J. Lataille
Ronald J. Lataille
Chief Financial Officer
(Principal Financial Officer)

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