

TERADYNE, INC
Form 10-Q
November 08, 2013
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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 September 29, 2013

OR

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

For the transition period from to

Commission File No. 001-06462

TERADYNE, INC.

(Exact name of registrant as specified in its charter)

Massachusetts
(State or Other Jurisdiction of

04-2272148
(I.R.S. Employer

Incorporation or Organization)

Identification No.)

600 Riverpark Drive, North Reading,

Massachusetts
(Address of Principal Executive Offices)

01864
(Zip Code)

978-370-2700

(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to the filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files) Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a 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

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

The number of shares outstanding of the registrant's only class of Common Stock as of November 1, 2013 was 191,611,017 shares.

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Table of Contents**PART I****Item 1: Financial Statements****TERADYNE, INC.****CONDENSED CONSOLIDATED BALANCE SHEETS****(Unaudited)**

	September 29, 2013	December 31, 2012
	(in thousands,	
	except per share information)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 572,868	\$ 338,920
Marketable securities	384,334	431,516
Accounts receivable, less allowance for doubtful accounts of \$3,562 and \$4,118 at September 29, 2013 and December 31, 2012, respectively	209,386	153,423
Inventories:		
Parts	70,620	89,598
Assemblies in process	25,923	32,303
Finished goods	26,489	17,509
	123,032	139,410
Deferred tax assets	83,780	77,305
Prepayments	109,107	90,931
Other current assets	11,873	4,556
Total current assets	1,494,380	1,236,061
Net property, plant and equipment	275,421	265,782
Long-term marketable securities	202,087	235,872
Other assets	19,763	20,209
Retirement plans assets	5,020	3,282
Intangible assets, net	265,705	318,867
Goodwill	349,272	349,272
Total assets	\$ 2,611,648	\$ 2,429,345
LIABILITIES		
Current liabilities:		
Accounts payable	\$ 67,734	\$ 58,324
Accrued employees compensation and withholdings	78,616	86,264
Deferred revenue and customer advances	70,367	81,357
Other accrued liabilities	62,184	57,249
Accrued income taxes	25,249	12,306
Current debt	183,573	2,328
Total current liabilities	487,723	297,828
Long-term deferred revenue and customer advances	17,455	16,227
Retirement plans liabilities	95,982	94,373
Deferred tax liabilities	37,632	50,201
Long-term other accrued liabilities	21,355	21,302
Long-term debt		171,059

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Total liabilities	660,147	650,990
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Commitments and contingencies (Note N)

SHAREHOLDERS EQUITY

Common stock, \$0.125 par value, 1,000,000 shares authorized, 191,399 shares and 187,908 shares issued and outstanding at September 29, 2013 and December 31, 2012, respectively	23,925	23,488
Additional paid-in capital	1,379,832	1,347,762
Accumulated other comprehensive income	3,855	5,820
Retained earnings	543,889	401,285
Total shareholders equity	1,951,501	1,778,355
Total liabilities and shareholders equity	\$ 2,611,648	\$ 2,429,345

The accompanying notes, together with the Notes to Consolidated Financial Statements included in Teradyne's Annual Report on Form 10-K for the year ended December 31, 2012, are an integral part of the condensed consolidated financial statements.

Table of Contents**TERADYNE, INC.****CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS****(Unaudited)**

	For the Three Months Ended		For the Nine Months Ended	
	September 29, 2013	September 30, 2012	September 29, 2013	September 30, 2012
	(in thousands, except per share amount)			
Net revenues:				
Products	\$ 365,825	\$ 393,037	\$ 943,212	\$ 1,204,506
Services	67,551	70,357	199,420	203,840
Total net revenues	433,376	463,394	1,142,632	1,408,346
Cost of revenues:				
Cost of products	150,365	169,782	405,569	550,282
Cost of services	28,717	33,412	88,119	97,432
Total cost of revenues	179,082	203,194	493,688	647,714
Gross profit	254,294	260,200	648,944	760,632
Operating expenses:				
Engineering and development	68,918	63,946	199,442	193,059
Selling and administrative	72,917	69,030	210,037	207,727
Acquired intangible assets amortization	18,064	18,429	54,163	55,287
Restructuring and other	889	683	1,480	(7,404)
Total operating expenses	160,788	152,088	465,122	448,669
Income from operations	93,506	108,112	183,822	311,963
Interest income	948	1,067	2,923	2,834
Interest expense and other	(6,902)	(6,154)	(20,262)	(18,536)
Income before income taxes	87,552	103,025	166,483	296,261
Income tax provision	18,093	14,384	23,879	62,669
Net income	\$ 69,459	\$ 88,641	\$ 142,604	\$ 233,592
Net income per common share:				
Basic	\$ 0.36	\$ 0.47	\$ 0.75	\$ 1.25
Diluted	\$ 0.29	\$ 0.39	\$ 0.61	\$ 1.02
Weighted average common shares basic	191,307	187,364	190,521	186,592
Weighted average common shares diluted	235,828	229,210	235,165	230,003

The accompanying notes, together with the Notes to Consolidated Financial Statements included in Teradyne's Annual Report on Form 10-K for the year ended December 31, 2012, are an integral part of the condensed consolidated financial statements.

Table of Contents**TERADYNE, INC.****CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME****(Unaudited)**

	For the Three Months Ended		For the Nine Months Ended	
	September 29, 2013	September 30, 2012	September 29, 2013	September 30, 2012
	(in thousands)			
Net income	\$ 69,459	\$ 88,641	\$ 142,604	\$ 233,592
Other comprehensive income:				
Available-for-sale marketable securities:				
Net unrealized gains (losses) on marketable securities arising during period	887	1,259	(1,019)	2,455
Less: Reclassification adjustment for net gains included in net income	(202)	(93)	(621)	(583)
Net change	685	1,166	(1,640)	1,872
Defined benefit pension and post-retirement plans:				
Amortization of prior service net benefit included in net periodic pension cost and post-retirement benefit	(109)	(92)	(325)	(275)
Other comprehensive income (loss)	576	1,074	(1,965)	1,597
Comprehensive income	\$ 70,035	\$ 89,715	\$ 140,639	\$ 235,189

The accompanying notes, together with the Notes to Consolidated Financial Statements included in Teradyne's Annual Report on Form 10-K for the year ended December 31, 2012, are an integral part of the condensed consolidated financial statements.

Table of Contents**TERADYNE, INC.****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited)**

	For the Nine Months Ended	
	September 29, 2013	September 30, 2012
	(in thousands)	
Cash flows from operating activities:		
Net income	\$ 142,604	\$ 233,592
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	41,873	39,812
Amortization	69,495	67,366
Stock-based compensation	27,227	30,634
Provision for excess and obsolete inventory	9,616	16,408
Deferred taxes	(19,211)	7,076
Non cash charge for the sale of inventories revalued at the date of acquisition		6,089
Contingent consideration adjustment		(8,373)
Tax benefit related to stock options and restricted stock units	(807)	(7,600)
Retirement plans actuarial (gains) losses	(1,359)	4,991
Impairment loss on property, plant and equipment	1,074	
Other	83	(2,359)
Changes in operating assets and liabilities:		
Accounts receivable	(55,963)	(76,134)
Inventories	34,194	25,070
Prepayments and other assets	(26,312)	7,278
Accounts payable and other accrued expenses	496	(17,600)
Deferred revenue and customer advances	(9,762)	(10,651)
Retirement plans contributions	(3,569)	(3,679)
Accrued income taxes	13,750	50,313
Net cash provided by operating activities	223,429	362,233
Cash flows from investing activities:		
Purchases of property, plant and equipment	(82,925)	(91,132)
Purchases of marketable securities	(657,188)	(510,157)
Proceeds from maturities of marketable securities	401,901	156,422
Proceeds from sales of marketable securities	332,597	14,250
Net cash used for investing activities	(5,615)	(430,617)
Cash flows from financing activities:		
Issuance of common stock under employee stock option and stock purchase plans	16,778	17,959
Tax benefit related to stock options and restricted stock units	807	7,600
Payments of long-term debt	(1,063)	(1,246)
Payments of contingent consideration	(388)	(43,973)
Net cash provided by (used) for financing activities	16,134	(19,660)
Increase (decrease) in cash and cash equivalents	233,948	(88,044)
Cash and cash equivalents at beginning of period	338,920	573,736
Cash and cash equivalents at end of period	\$ 572,868	\$ 485,692

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TERADYNE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

A. The Company

Teradyne, Inc. (the Company or Teradyne) is a leading global supplier of automatic test equipment. Teradyne's automatic test equipment products and services include:

semiconductor test (Semiconductor Test) systems;

wireless test (Wireless Test) systems; and

military/aerospace (Mil/Aero) test instrumentation and systems, storage test (Storage Test) systems, and circuit-board test and inspection (Commercial Board Test) systems, collectively these products represent System Test .

B. Accounting Policies

Basis of Presentation

The condensed consolidated interim financial statements include the accounts of Teradyne and its wholly-owned subsidiaries. All significant intercompany balances and transactions have been eliminated. These interim financial statements are unaudited and reflect all normal recurring adjustments that are, in the opinion of management, necessary for the fair presentation of such interim financial statements. Certain prior year amounts were reclassified to conform to the current year presentation. The December 31, 2012 condensed consolidated balance sheet data was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America.

The accompanying financial information should be read in conjunction with the consolidated financial statements and notes thereto contained in Teradyne's Annual Report on Form 10-K, filed with the U.S. Security and Exchange Commission (SEC) on March 1, 2013, for the year ended December 31, 2012.

Preparation of Financial Statements and Use of Estimates

The preparation of consolidated financial statements requires management to make estimates and judgments that affect the amounts reported in the financial statements. Actual results may differ significantly from these estimates.

C. Recently Issued Accounting Pronouncements

In December 2011, the Financial Accounting Standards Board (FASB) issued Accounting Standard Update (ASU) No. 2011-11, *Disclosures about Offsetting Assets and Liabilities*. This ASU is intended to enhance the understanding of the effects of netting arrangements on an entity's financial statements, including financial instruments and derivative instruments that are either offset or subject to a master netting arrangement. The scope of this ASU includes derivatives, sale and repurchase agreements, reverse sale and repurchase agreements, and securities borrowing and lending arrangements. The provisions of this ASU are effective for interim and annual periods beginning on or after January 1, 2013. Teradyne adopted this ASU effective January 1, 2013. See Note D Financial Instruments and Derivatives.

In February 2013, the FASB issued ASU 2013-02, *Comprehensive Income (Topic 220): Reporting of Amounts Reclassified out of Accumulated Other Comprehensive Income* amending the disclosure requirements regarding the reporting of amounts reclassified out of accumulated other comprehensive income. The amendment

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does not change the current requirement for reporting net income or other comprehensive income, but requires additional disclosures about significant amounts reclassified out of accumulated other comprehensive income including the effect of the reclassification on the related statement of operations line items. The provisions of this ASU are effective for interim and annual periods beginning on or after January 1, 2013. Teradyne adopted this amendment effective January 1, 2013. See Note I Accumulated Other Comprehensive Income.

On July 18, 2013, the FASB issued ASU 2013-11, *Income Taxes (Topic 740): Presentation of an Unrecognized Tax Benefit When a Net Operating Loss Carryforward, a Similar Tax Loss, or a Tax Credit Carryforward Exists*. Under this ASU, unrecognized tax benefits will be netted against all available same-jurisdiction loss or other tax carryforwards that would be utilized, rather than only against carryforwards that are created by unrecognized tax benefits. The provisions of this ASU are effective for interim and annual periods beginning on or after December 15, 2013. Teradyne does not expect this ASU to have a material impact on its financial position or results of operations.

D. Financial Instruments and Derivatives

Financial Instruments

Teradyne uses the market and income approach to value its financial instruments and there was no change in valuation techniques used by Teradyne during the three and nine months ended September 29, 2013 and September 30, 2012. As defined in ASC 820-10, *Fair Value Measurements and Disclosures*, fair value is the price that would be received from the sale of an asset or paid to transfer a liability in an orderly transaction between market participants. ASC 820-10 requires that assets and liabilities are carried at fair value and are classified in one of the following three categories:

Level 1: Quoted prices in active markets for identical assets as of the reporting date.

Level 2: Inputs other than Level 1, that are observable either directly or indirectly as of the reporting date. For example, a common approach for valuing fixed income securities is the use of matrix pricing. Matrix pricing is a mathematical technique used to value securities by relying on the securities' relationship to other benchmark quoted prices.

Level 3: Unobservable inputs that are not supported by market data. Unobservable inputs are developed based on the best information available, which might include Teradyne's own data.

Most of Teradyne's fixed income securities are classified as Level 2, with the exception of U.S. Treasury securities and investments in equity and debt mutual funds, which are classified as Level 1, and contingent consideration, which is classified as Level 3. The majority of Level 2 securities are priced by third party pricing vendors. These pricing vendors utilize the most recent observable market information in pricing these securities or, if specific prices are not available, use other observable inputs like market transactions involving identical or comparable securities.

There were no realized losses recorded in the three and nine months ended September 29, 2013 and September 30, 2012. Realized gains recorded in the three and nine months ended September 29, 2013, were \$0.2 million and \$0.5 million, respectively. Realized gains recorded in the three and nine months ended September 30, 2012, were \$0.3 million and \$0.9 million, respectively. Realized gains are included in interest income.

During the nine months ended September 29, 2013 and September 30, 2012, there were no transfers in or out of Level 1, Level 2 or Level 3 financial instruments.

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The following table sets forth by fair value hierarchy Teradyne's financial assets and liabilities that were measured at fair value on a recurring basis as of September 29, 2013 and December 31, 2012.

	September 29, 2013			Total
	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
	(in thousands)			
Assets				
Cash	\$ 147,819	\$	\$	\$ 147,819
Cash equivalents	417,823	7,226		425,049
Available-for-sale securities:				
U.S. government agency securities		229,129		229,129
U.S. Treasury securities	211,956			211,956
Commercial paper		88,891		88,891
Corporate debt securities		43,982		43,982
Equity and debt mutual funds	12,122			12,122
Certificates of deposit and time deposits		261		261
Non-U.S. government securities		80		80
Total	789,720	369,569		1,159,289
Derivatives		276		276
Total	\$ 789,720	\$ 369,845	\$	\$ 1,159,565

Reported as follows:

	(Level 1)	(Level 2)	(Level 3)	Total
	(in thousands)			
Assets				
Cash and cash equivalents	\$ 565,642	\$ 7,226	\$	\$ 572,868
Marketable securities	185,085	199,249		384,334
Long-term marketable securities	38,993	163,094		202,087
Other current assets		276		276
Total	\$ 789,720	\$ 369,845	\$	\$ 1,159,565

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	December 31, 2012			Total
	Quoted Prices in Active Markets for Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
	(in thousands)			
Assets				
Cash	\$ 139,354	\$	\$	\$ 139,354
Cash equivalents	183,039	16,527		199,566
Available-for-sale securities:				
U.S. Treasury securities	312,116			312,116
U.S. government agency securities		217,655		217,655
Commercial paper		70,434		70,434
Corporate debt securities		55,755		55,755
Equity and debt mutual funds	9,717			9,717
Certificates of deposit and time deposits		1,627		1,627
Non-U.S. government securities		84		84
Total	644,226	362,082		1,006,308
Derivatives				
		121		121
Total	\$ 644,226	\$ 362,203	\$	\$ 1,006,429
Liabilities				
Contingent consideration	\$	\$	\$ 388	\$ 388
Total	\$	\$	\$ 388	\$ 388

Reported as follows:

	(Level 1)	(Level 2)	(Level 3)	Total
	(in thousands)			
Assets				
Cash and cash equivalents	\$ 322,393	\$ 16,527	\$	\$ 338,920
Marketable securities	239,192	192,324		431,516
Long-term marketable securities	82,641	153,231		235,872
Other current assets		121		121
	\$ 644,226	\$ 362,203	\$	\$ 1,006,429
Liabilities				
Other accrued liabilities	\$	\$	\$ 388	\$ 388
	\$	\$	\$ 388	\$ 388

During the nine months ended September 29, 2013, Teradyne made the final payment for Level 3 contingent consideration of \$0.4 million.

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The carrying amounts and fair values of financial instruments at September 29, 2013 and December 31, 2012 were as follows:

	September 29, 2013		December 31, 2012	
	Carrying Value	Fair Value	Carrying Value	Fair Value
	(in thousands)			
Cash and cash equivalents	\$ 572,868	\$ 572,868	\$ 338,920	\$ 338,920
Marketable securities	586,421	586,421	667,388	667,388
Convertible debt(1)	181,550	580,206	169,896	589,000
Japan loan	2,023	2,023	3,491	3,491

(1) The carrying value represents the bifurcated debt component only, while the fair value is based on quoted market prices for the convertible note which includes the equity conversion feature.

The fair values of cash and cash equivalents, accounts receivable, net and accounts payable approximate the carrying amount due to the short-term nature of these instruments.

The following tables summarize the composition of available-for-sale marketable securities at September 29, 2013 and December 31, 2012:

	September 29, 2013				Fair Market Value of Investments with Unrealized Losses
	Cost	Unrealized Gain	Unrealized (Loss)	Fair Market Value	
	(in thousands)				
U.S. government agency securities	\$ 229,133	\$ 142	\$ (146)	\$ 229,129	\$ 103,165
U.S. Treasury securities	211,966	140	(150)	211,956	5,605
Commercial paper	88,884	12	(5)	88,891	25,169
Corporate debt securities	44,132	905	(1,055)	43,982	16,439
Equity and debt mutual funds	9,843	2,315	(36)	12,122	595
Certificates of deposit and time deposits	261			261	
Non-U.S. government securities	80			80	
	\$ 584,299	\$ 3,514	\$ (1,392)	\$ 586,421	\$ 150,973

Reported as follows:

	Cost	Unrealized Gain	Unrealized (Loss)	Fair Market Value	Fair Market Value of Investments with Unrealized Losses
	(in thousands)				
Marketable securities	\$ 384,180	\$ 168	\$ (14)	\$ 384,334	\$ 37,823
Long-term marketable securities	200,119	3,346	(1,378)	202,087	113,150
	\$ 584,299	\$ 3,514	\$ (1,392)	\$ 586,421	\$ 150,973

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	December 31, 2012				Fair Market Value of Investments with Unrealized Losses
	Available-for-Sale				
	Cost	Unrealized Gain	Unrealized (Loss) (in thousands)	Fair Market Value	
U.S. Treasury securities	\$ 311,915	\$ 216	\$ (15)	\$ 312,116	\$ 1,018
U.S. government agency securities	217,396	262	(3)	217,655	9,018
Commercial paper	70,431	9	(6)	70,434	25,209
Corporate debt securities	53,405	2,414	(64)	55,755	23,255
Equity and debt mutual funds	8,767	961	(11)	9,717	600
Certificates of deposit and time deposits	1,627			1,627	
Non-U.S. government securities	84			84	
	\$ 663,625	\$ 3,862	\$ (99)	\$ 667,388	\$ 59,100

Reported as follows:

	Cost	Unrealized Gain	Unrealized (Loss) (in thousands)	Fair Market Value	Fair Market Value of Investments with Unrealized Losses
Marketable securities	\$ 431,324	\$ 203	\$ (11)	\$ 431,516	\$ 41,110
Long-term marketable securities	232,301	3,659	(88)	235,872	17,990
	\$ 663,625	\$ 3,862	\$ (99)	\$ 667,388	\$ 59,100

As of September 29, 2013, the fair market value of marketable securities with unrealized losses totaled \$151.0 million. Of this value, \$0.5 million had unrealized losses greater than one year and \$150.5 million had unrealized losses less than one year. As of December 31, 2012, the fair market value of marketable securities with unrealized losses totaled \$59.1 million and none of the unrealized losses were greater than one year.

The contractual maturities of available-for-sale marketable securities at September 29, 2013 were as follows:

	September 29, 2013	
	Cost	Fair Market Value
	(in thousands)	
Due within one year	\$ 384,180	\$ 384,334
Due after 1 year through 5 years	173,407	175,657
Due after 5 years through 10 years	3,131	3,188
Due after 10 years	23,581	23,242
Total	\$ 584,299	\$ 586,421

Derivatives

Teradyne conducts business in a number of foreign countries, with certain transactions denominated in local currencies. The purpose of Teradyne's foreign currency management is to minimize the effect of exchange rate fluctuations on certain foreign currency denominated net

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monetary assets. Teradyne does not use derivative financial instruments for trading or speculative purposes.

To minimize the effect of exchange rate fluctuations associated with the remeasurement of monetary assets and liabilities denominated in foreign currencies, Teradyne enters into foreign currency forward contracts. The change in fair value of these derivatives is recorded directly in earnings, and is used to offset the change in fair value of the monetary assets and liabilities denominated in foreign currencies.

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The notional amount of foreign exchange contracts hedging monetary assets and liabilities denominated in foreign currencies was \$64.1 million and \$64.1 million at September 29, 2013 and December 31, 2012, respectively.

The following table summarizes the fair value of derivative instruments at September 29, 2013 and December 31, 2012:

	Balance Sheet Location	September 29, 2013	December 31, 2012
(in thousands)			
Derivatives not designated as hedging instruments:			
Foreign exchange contracts	Other current assets	\$ 276	\$ 121
		\$ 276	\$ 121

Teradyne had no offsetting foreign exchange contracts at September 29, 2013 and December 31, 2012.

The following table summarizes the effect of derivative instruments recognized in the statement of operations during the three and nine months ended September 29, 2013 and September 30, 2012. The table does not reflect the corresponding (losses) gains from the remeasurement of the monetary assets and liabilities denominated in foreign currencies. For the three and nine months ended September 29, 2013, losses from the remeasurement of the monetary assets and liabilities denominated in foreign currencies were \$(0.4) million and \$(5.0) million, respectively. For the three and nine months ended September 30, 2012, gains from the remeasurement of the monetary assets and liabilities denominated in foreign currencies were \$1.2 million and \$0.8 million, respectively.

	Location of Gains (Losses) Recognized in Statement of Operations	For the Three Months Ended		For the Nine Months Ended	
		September 29, 2013	September 30, 2012	September 29, 2013	September 30, 2012
(in thousands)					
Derivatives not designated as hedging instruments:					
Foreign exchange contracts	Interest expense and other	\$ 1	\$ (1,197)	\$ 4,068	\$ (677)
		\$ 1	\$ (1,197)	\$ 4,068	\$ (677)

See Note E Debt regarding derivatives related to convertible senior notes.

E. Debt**Loan Agreement**

On March 31, 2009, Teradyne K.K., Teradyne's wholly-owned subsidiary in Japan, entered into a loan agreement with a local bank in Japan to borrow approximately \$10.0 million (the loan is denominated in Japanese Yen). The loan has a term of 5 years and a fixed interest rate of 0.8%. Approximately \$6.0 million of the loan is collateralized by a real estate mortgage on Teradyne K.K.'s building and land in Kumamoto, Japan and approximately \$4.0 million is unsecured. Teradyne, Inc. has guaranteed payment of the loan obligation. The loan is amortized over the term of the loan with semiannual principal payments of approximately \$1.0 million payable on September 30 and March 30 each year. At September 29, 2013, the outstanding loan principal of approximately \$2.0 million is included in current debt.

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In April 2009, Teradyne issued 4.50% convertible senior notes (the "Notes") at an aggregate principal amount of \$190 million. The Notes will mature on March 15, 2014, unless earlier repurchased by Teradyne or converted. The Notes are senior unsecured obligations and rank equally with all of Teradyne's existing and future senior debt and senior to any of Teradyne's subordinated debt.

The Notes may be converted, at the option of the holder, under certain circumstances and during certain periods, at an initial conversion rate of approximately 182.65 shares of Teradyne's common stock per \$1,000 principal amount of Notes, which is equivalent to an initial conversion price of approximately \$5.48, a 25% conversion premium based on the last reported sale price of \$4.38 per share of Teradyne's common stock on March 31, 2009. The conversion rate is subject to adjustment in certain circumstances including but not limited to Teradyne issuing a cash or stock dividend or effecting a stock split.

During the three months ended September 29, 2013, the following circumstance occurred that allows holders to convert their Notes at their option prior to December 15, 2013: the last reported sale price of Teradyne's common stock for 20 or more trading days in a period of 30 consecutive trading days ending on the last trading day of the immediately preceding calendar quarter exceeded 130% of the conversion price in effect on the last trading day of the immediately preceding calendar quarter. As of November 8, 2013, one holder exercised the option to convert two thousand dollars worth of Notes which Teradyne settled in cash.

Concurrently with the offering of the Notes, Teradyne entered into a convertible note hedge transaction with a strike price equal to the initial conversion price of the Notes, or approximately \$5.48. The convertible note hedge allows Teradyne to receive shares of its common stock and/or cash related to the excess conversion value that it would pay to the holders of the Notes upon conversion. The convertible note hedges will cover, subject to customary antidilution adjustments, approximately 34,703,196 shares of Teradyne's common stock. Teradyne paid approximately \$64.6 million for the convertible note hedges.

On March 31, 2009, Teradyne entered into a warrant transaction with a strike price of approximately \$7.67 per share, which was 75% higher than the closing price of Teradyne's common stock. Teradyne received approximately \$43.0 million for the warrants.

The convertible note hedge and warrant transaction will generally have the effect of increasing the conversion price of the Notes to approximately \$7.67 per share of Teradyne's common stock, representing a 75% conversion premium based upon the closing price of Teradyne's common stock on March 31, 2009.

The Notes are classified as current debt in the balance sheet at September 29, 2013. The tables below represent the components of Teradyne's convertible senior notes:

	September 29, 2013	December 31, 2012
	(in thousands)	
Debt principal	\$ 189,998	\$ 190,000
Unamortized debt discount	8,448	20,104
Net carrying amount of the convertible debt	\$ 181,550	\$ 169,896

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The interest expense on Teradyne's convertible senior notes for the three and nine months ended September 29, 2013 and September 30, 2012 was as follows:

	For the Three Months Ended		For the Nine Months Ended	
	September 29, 2013	September 30, 2012	September 29, 2013	September 30, 2012
	(in thousands)			
Contractual interest expense	\$ 2,114	\$ 2,114	\$ 6,388	\$ 6,413
Amortization of the discount component and debt issue fees	4,221	3,710	12,266	10,781
Total interest expense on the convertible debt	\$ 6,335	\$ 5,824	\$ 18,654	\$ 17,194

As of September 29, 2013, the unamortized discount was \$8.4 million, which will be amortized over the next six months, and the carrying amount of the equity component was \$63.4 million. As of September 29, 2013, the conversion rate was equal to the initial conversion price of approximately \$5.48 per share and the if-converted value of the Notes was \$579.9 million.

F. Deferred Revenue and Customer Advances

Deferred revenue and customer advances consist of the following and are included in short and long-term deferred revenue and customer advances.

	September 29, 2013	December 31, 2012
	(in thousands)	
Maintenance, training and extended warranty	\$ 56,481	\$ 51,198
Customer advances	22,287	39,613
Undelivered elements	9,054	6,773
Total deferred revenue and customer advances	\$ 87,822	\$ 97,584

G. Product Warranty

Teradyne generally provides a one-year warranty on its products commencing upon installation or shipment. A provision is recorded upon revenue recognition to cost of revenues for estimated warranty expense based on historical experience. Related costs are charged to the warranty accrual as incurred. The warranty balance below is included in other accrued liabilities.

	For the Three Months Ended		For the Nine Months Ended	
	September 29, 2013	September 30, 2012	September 29, 2013	September 30, 2012
	(in thousands)			
Balance at beginning of period	\$ 7,351	\$ 11,047	\$ 9,786	\$ 8,154
Accruals for warranties issued during the period	3,674	4,118	8,781	13,543
Adjustments related to pre-existing warranties	(524)	1,226	(2,323)	1,369
Settlements made during the period	(2,470)	(3,813)	(8,213)	(10,488)
Balance at end of period	\$ 8,031	\$ 12,578	\$ 8,031	\$ 12,578

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When Teradyne receives revenue for extended warranty beyond one year, it is deferred and recognized on a straight-line basis over the contract period. Related costs are expensed as incurred. The extended warranty balance below is included in short and long-term deferred revenue and customer advances.

	For the Three Months Ended		For the Nine Months Ended	
	September 29, 2013	September 30, 2012	September 29, 2013	September 30, 2012
	(in thousands)			
Balance at beginning of period	\$ 34,854	\$ 20,754	\$ 26,987	\$ 12,742
Deferral of new extended warranty revenue	5,586	8,733	17,791	21,015
Recognition of extended warranty deferred revenue	(4,120)	(2,007)	(8,458)	(6,277)
Balance at end of period	\$ 36,320	\$ 27,480	\$ 36,320	\$ 27,480

H. Stock-Based Compensation

Restricted stock unit awards granted to employees vest in equal installments over four years. A portion of restricted stock unit awards granted to executive officers is subject to time-based vesting and a portion is subject to performance-based vesting. The percentage level of performance satisfied for performance-based grants is assessed on or near the anniversary of the grant date and, in turn, that percentage level determines the number of performance-based restricted stock units available for vesting over the vesting period; portions of the performance-based grants not available for vesting will be forfeited. Stock options vest in equal installments over four years, and have a term of seven years from the date of grant.

During the nine months ended September 29, 2013, Teradyne granted 1.9 million of restricted stock unit awards to employees at a weighted average grant date fair value of \$16.60 and 0.2 million of service-based stock options to executive officers at a weighted average grant date fair value of \$6.09.

During the nine months ended September 30, 2012, Teradyne granted 1.7 million of restricted stock unit awards to employees at a weighted average grant date fair value of \$16.73 and 0.2 million of service-based stock options to executive officers at a weighted average grant date fair value of \$6.85.

The fair value of stock options was estimated using the Black-Scholes option-pricing model with the following assumptions:

	For the Nine Months Ended	
	September 29, 2013	September 30, 2012
Expected life (years)	4.0	3.5
Interest rate	0.6%	0.4%
Volatility-historical	46.8%	56.0%
Dividend yield	0.0%	0.0%

Teradyne determined the stock options' expected life based upon historical exercise data for executive officers, the age of the executive officers and the terms of the stock option grant. Volatility was determined using historical volatility for a period equal to the expected life. The risk-free rate was determined using the U.S. Treasury yield curve in effect at the time of grant.

Effective January 1, 2013, the price paid by employees for Teradyne's common stock purchased through the employee stock purchase plan is equal to 85% of the stock price on the last business day of the purchase period.

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During 2012, the price paid by employees for Teradyne's common stock purchased through the employee stock purchase plan was equal to 85% of the lower of the stock price on the first or last business day of the purchase period.

The weighted-average fair value of employee stock purchase rights granted in the nine months ended September 30, 2012 was \$3.75. The fair value of the employees' purchase rights granted in the nine months ended September 30, 2012 was estimated using the Black-Scholes option-pricing model with the following assumptions:

	For the Nine Months Ended September 30, 2012
Expected life (years)	0.5
Interest rate	0.11%
Volatility-historical	42.7%
Dividend yield	0.0%

I. Accumulated Other Comprehensive Income

Changes in accumulated other comprehensive income, which is presented net of tax, consist of the following:

	Unrealized Gains on Marketable Securities	Retirement Plans Prior Service Credit (in thousands)	Total
Balance at December 31, 2012 (a)	\$ 2,925	\$ 2,895	\$ 5,820
Other comprehensive income before reclassifications	(1,019)		(1,019)
Amounts reclassified from accumulated other comprehensive income	(621)	(325)	(946)
Net current period other comprehensive income	(1,640)	(325)	(1,965)
Balance at September 29, 2013 (a)	\$ 1,285	\$ 2,570	\$ 3,855

(a) Net of tax of \$835 for unrealized gains on marketable securities and \$(125) for retirement plans prior service credit. Reclassifications out of accumulated other comprehensive income to the statement of operations for the three and nine months ended September 29, 2013 and September 30, 2012, were as follows:

Details about Accumulated

Other Comprehensive Income

Components	For the Three Months Ended		For the Nine Months Ended		Affected Line Item in the Statements of Operations
	September 29, 2013	September 30, 2012	September 29, 2013	September 30, 2012	
Available-for-sale marketable securities					
Unrealized gains	\$ 202	\$ 93	\$ 621	\$ 583	Interest income
	\$ 202	\$ 93	\$ 621	\$ 583	
Amortization of defined benefit pension and postretirement plans	\$ 109	\$ 92	\$ 325	\$ 275	(a)

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Prior service benefit					
	\$ 109	\$ 92	\$ 325	\$ 275	
Total reclassifications	\$ 311	\$ 185	\$ 946	\$ 858	Net income

- (a) The amortization of prior service benefit is included in the computation of net periodic pension cost and postretirement benefit; see Note M Retirement Plans.

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J. Intangible Assets

Amortizable intangible assets consist of the following and are included in intangible assets, net on the balance sheet:

	Gross Carrying Amount	September 29, 2013		Weighted Average Useful Life
		Accumulated Amortization (in thousands)	Net Carrying Amount	
Developed technology	\$ 358,555	\$ 180,960	\$ 177,595	6.3 years
Customer relationships and service and software maintenance contracts	144,971	77,139	67,832	8.0 years
Trade names and trademarks	33,840	13,562	20,278	9.0 years
Customer backlog	1,000	1,000		0.4 years
Total intangible assets	\$ 538,366	\$ 272,661	\$ 265,705	7.0 years

	Gross Carrying Amount	December 31, 2012		Weighted Average Useful Life
		Accumulated Amortization (in thousands)	Net Carrying Amount	
Developed technology	\$ 357,555	\$ 143,126	\$ 214,429	6.3 years
Customer relationships and service and software maintenance contracts	144,971	63,464	81,507	8.0 years
Trade names and trademarks	33,840	10,909	22,931	9.0 years
Customer backlog	1,000	1,000		0.4 years
Total intangible assets	\$ 537,366	\$ 218,499	\$ 318,867	7.0 years

Aggregate intangible asset amortization expense was \$18.1 million and \$54.2 million, respectively, for the three and nine months ended September 29, 2013 and \$18.4 million and \$55.3 million, respectively, for the three and nine months ended September 30, 2012. Estimated intangible asset amortization expense for each of the five succeeding fiscal years is as follows:

Year	Amortization Expense (in thousands)
2013 (remainder)	\$ 18,052
2014	69,213
2015	52,462
2016	52,462
2017	46,304

Table of Contents**K. Net Income per Common Share**

The following table sets forth the computation of basic and diluted net income per common share:

	For the Three Months Ended		For the Nine Months Ended	
	September 29, 2013	September 30, 2012	September 29, 2013	September 30, 2012
	(in thousands, except per share amounts)			
Net income for basic and diluted net income per share	\$ 69,459	\$ 88,641	\$ 142,604	\$ 233,592
Weighted average common shares-basic	191,307	187,364	190,521	186,592
Effect of dilutive potential common shares:				
Incremental shares from assumed conversion of convertible notes(1)	23,257	21,890	23,303	22,397
Convertible note hedge warrant shares(2)	18,678	16,765	18,742	17,474
Restricted stock units	1,102	1,423	1,000	1,413
Stock options	1,465	1,735	1,564	2,075
Employee stock purchase rights	19	33	35	52
				