

R F INDUSTRIES LTD
Form 10-Q
September 11, 2015

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

Form 10-Q

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended July 31, 2015

Commission file number: **0-13301**

RF INDUSTRIES, LTD.

(Exact name of registrant as specified in its charter)

Nevada
(State or other jurisdiction of incorporation or organization)

88-0168936
(I.R.S. Employer Identification No.)

7610 Miramar Road, Building 6000
San Diego, California
(Address of principal executive offices)

92126
(Zip Code)

(858) 549-6340

(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 such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T 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, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" 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 of the issuer's Common Stock, par value \$0.01 per share, outstanding as of September 8, 2015 was 8,571,831.

Part I. FINANCIAL INFORMATION**Item 1: Financial Statements****RF INDUSTRIES, LTD. AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS****(In thousands, except share and per share amounts)**

| | July 31, 2015 (Unaudited) | October 31, 2014 (Note 1) |
|--|--|--|
| ASSETS | | |
| CURRENT ASSETS | | |
| Cash and cash equivalents | \$ 7,908 | \$ 14,718 |
| Trade accounts receivable, net of allowance for doubtful accounts of \$47 and \$30 | 3,915 | 2,428 |
| Inventories | 7,263 | 5,259 |
| Other current assets | 1,041 | 618 |
| Deferred tax assets | 416 | 416 |
| TOTAL CURRENT ASSETS | 20,543 | 23,439 |
| Property and equipment: | | |
| Equipment and tooling | 3,153 | 2,610 |
| Furniture and office equipment | 970 | 777 |
| | 4,123 | 3,387 |
| Less accumulated depreciation | 3,161 | 2,558 |
| Total property and equipment | 962 | 829 |
| Goodwill | 5,913 | 3,076 |
| Amortizable intangible assets, net | 4,440 | 1,187 |
| Non-amortizable intangible assets | 1,387 | 410 |
| Note receivable from stockholder | 67 | 67 |
| Other assets | 38 | 21 |
| TOTAL ASSETS | \$ 33,350 | \$ 29,029 |

See Notes to Unaudited Condensed Consolidated Financial Statements.

Item 1: Financial Statements (continued)**RF INDUSTRIES, LTD. AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS**

(In thousands, except share and per share amounts)

| | July 31, 2015 (Unaudited) | October 31, 2014 (Note 1) |
|--|--|--|
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| CURRENT LIABILITIES | | |
| Accounts payable | \$ 1,979 | \$ 867 |
| Accrued expenses | 2,882 | 1,422 |
| Income taxes payable | - | 73 |
| TOTAL CURRENT LIABILITIES | 4,861 | 2,362 |
| Deferred tax liabilities | 1,299 | 811 |
| Other long-term liabilities | 946 | - |
| TOTAL LIABILITIES | 7,106 | 3,173 |
| COMMITMENTS AND CONTINGENCIES | | |
| STOCKHOLDERS' EQUITY | | |
| Common stock - authorized 20,000,000 shares of \$0.01 par value; 8,571,831 and 8,255,979 shares issued and outstanding at July 31, 2015 and October 31, 2014, respectively | 86 | 83 |
| Additional paid-in capital | 18,664 | 17,230 |
| Retained earnings | 7,494 | 8,543 |
| TOTAL STOCKHOLDERS' EQUITY | 26,244 | 25,856 |
| TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY | \$ 33,350 | \$ 29,029 |

See Notes to Unaudited Condensed Consolidated Financial Statements.

Item 1: Financial Statements (continued)**RF INDUSTRIES, LTD. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF INCOME****(UNAUDITED)****(In thousands, except share and per share amounts)**

| | Three Months Ended July | | Nine Months Ended July | |
|---|--------------------------------|-------------|-------------------------------|-------------|
| | 31, | | 31, | |
| | 2015 | 2014 | 2015 | 2014 |
| Net sales | \$ 8,899 | \$ 5,536 | \$ 23,868 | \$ 17,150 |
| Cost of sales | 6,064 | 3,048 | 15,464 | 9,328 |
| Gross profit | 2,835 | 2,488 | 8,404 | 7,822 |
| Operating expenses: | | | | |
| Engineering | 247 | 228 | 688 | 697 |
| Selling and general | 2,455 | 1,632 | 6,833 | 5,395 |
| Totals | 2,702 | 1,860 | 7,521 | 6,092 |
| Operating income | 133 | 628 | 883 | 1,730 |
| Other income – interest | 5 | 7 | 19 | 22 |
| Income from continuing operations before provision for income taxes | 138 | 635 | 902 | 1,752 |
| Provision (benefit) for income taxes | (44 |) 277 | 220 | 670 |
| Income from continuing operations | 182 | 358 | 682 | 1,082 |
| Income from discontinued operations, net of tax | 29 | 14 | 42 | 32 |
| Net income | \$ 211 | \$ 372 | \$ 724 | \$ 1,114 |
| Earnings per share - Basic: | | | | |
| Continuing operations | \$ 0.02 | \$ 0.05 | \$ 0.08 | \$ 0.14 |
| Discontinued operations | 0.00 | 0.00 | 0.01 | 0.00 |
| Net income per share | \$ 0.02 | \$ 0.05 | \$ 0.09 | \$ 0.14 |

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Earnings per share - Diluted:

| | | | | |
|--------------------------------------|-----------|-----------|-----------|-----------|
| Continuing operations | \$ 0.02 | \$ 0.04 | \$ 0.08 | \$ 0.13 |
| Discontinued operations | 0.00 | 0.00 | 0.00 | 0.00 |
| Net income per share | \$ 0.02 | \$ 0.04 | \$ 0.08 | \$ 0.13 |
| Weighted average shares outstanding: | | | | |
| Basic | 8,545,300 | 8,250,042 | 8,446,223 | 8,200,476 |
| Diluted | 8,916,643 | 8,718,656 | 8,820,438 | 8,763,593 |

See Notes to Unaudited Condensed Consolidated Financial Statements.

Item 1: Financial Statements (continued)**RF INDUSTRIES, LTD. AND SUBSIDIARIES****CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(UNAUDITED)****(In thousands)**

| | Nine Months Ended July | |
|---|-------------------------------|-------------|
| | 31, | |
| | 2015 | 2014 |
| OPERATING ACTIVITIES: | | |
| Net income | \$ 724 | \$ 1,114 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Bad debt (recovery) expense | 15 | (36) |
| Accounts receivable write-off | 4 | 5 |
| Depreciation and amortization | 719 | 445 |
| Stock-based compensation expense | 184 | 323 |
| Inventory write-off | 10 | - |
| Excess tax benefit from stock-based compensation | 45 | (277) |
| Changes in operating assets and liabilities: | | |
| Trade accounts receivable | (323) | 602 |
| Inventories | (380) | 383 |
| Other current assets | (322) | 942 |
| Other long-term assets | - | 9 |
| Accounts payable | 133 | (95) |
| Income taxes prepaid (payable) | (122) | 277 |
| Accrued expenses | (444) | (305) |
| Net cash provided by operating activities | 243 | 3,387 |
| INVESTING ACTIVITIES: | | |
| Acquisition of businesses (Comnet, Rel-Tech and CompPro), net of cash acquired of (\$758) | (5,132) | - |
| Capital expenditures | (140) | (109) |
| Net cash used in investing activities | (5,272) | (109) |
| FINANCING ACTIVITIES: | | |
| Proceeds from exercise of stock options | 37 | 524 |
| Excess tax benefit from exercise of stock options | (45) | 277 |
| Dividends paid | (1,773) | (1,723) |
| Net cash used in financing activities | (1,781) | (922) |
| Net increase (decrease) in cash and cash equivalents | (6,810) | 2,356 |

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| | | |
|--|----------|-----------|
| Cash and cash equivalents, beginning of period | 14,718 | 11,881 |
| Cash and cash equivalents, end of period | \$ 7,908 | \$ 14,237 |
| Supplemental cash flow information – income taxes paid | \$ 627 | \$ - |
| Noncash investing and financing activities: | | |
| Write off of fully depreciated fixed assets | \$ - | \$ 14 |
| Stock issuance for acquisition of businesses (Comnet and Rel-Tech) | \$ 1,260 | \$ - |

See Notes to Unaudited Condensed Consolidated Financial Statements.

RF INDUSTRIES, LTD. AND SUBSIDIARIES

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

Note 1 - Unaudited interim condensed consolidated financial statements

The accompanying unaudited condensed consolidated financial statements have been prepared in conformity with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for complete financial statements. In the opinion of management, all adjustments, which are normal and recurring, have been included in order to make the information not misleading. Information included in the consolidated balance sheet as of October 31, 2014 has been derived from, and certain terms used herein are defined in, the audited financial statements of the Company as of October 31, 2014 included in the Company's Annual Report on Form 10-K ("Form 10-K") for the year ended October 31, 2014 that was previously filed with the Securities and Exchange Commission ("SEC"). Operating results for the three and nine month periods ended July 31, 2015 are not necessarily indicative of the results that may be expected for the year ending October 31, 2015. The unaudited condensed consolidated financial statements should be read in conjunction with the financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended October 31, 2014.

Principles of consolidation

The accompanying unaudited condensed consolidated financial statements for the periods ending on or before October 31, 2014 include the accounts of RF Industries, Ltd. and Cables Unlimited, Inc. ("Cables Unlimited"), a wholly-owned subsidiary. The unaudited condensed consolidated financial statements for the three and nine months ended July 31, 2015 include the accounts of RF Industries, Ltd., Cables Unlimited, Comnet Telecom Supply, Inc. ("Comnet"), a wholly-owned subsidiary that RF Industries, Ltd. acquired effective November 1, 2014 and Rel-Tech Electronics, Inc. ("Rel-Tech"), a wholly-owned subsidiary that RF Industries, Ltd. acquired effective June 1, 2015. For periods ending on or before October 31, 2014, references herein to the "Company" shall refer to RF Industries, Ltd. and Cables Unlimited, and for all periods after October 31, 2014, references to the "Company" shall refer to RF Industries, Ltd., Cables Unlimited, Comnet and Rel-Tech, collectively. All intercompany balances and transactions have been eliminated in consolidation.

Revenue recognition

Four basic criteria must be met before revenue can be recognized: (1) persuasive evidence of an arrangement exists; (2) delivery has occurred or services rendered; (3) the fee is fixed and determinable; and (4) collectability is reasonably assured. The Company recognizes revenue from product sales after purchase orders are received which contain a fixed price and the products are shipped. Most of the Company's products are sold to continuing customers with established credit histories.

Note 2 - Business Acquisitions

Rel-Tech Electronics, Inc.

On June 5, 2015, the Company purchased 100% of the issued and outstanding shares of Rel-Tech pursuant to a Stock Purchase Agreement. Rel-Tech is wholly-owned by Wilfred D, LeBlanc Jr., Ralph Palumbo and their respective wives. Rel-Tech is a Milford, Connecticut-based manufacturer and supplier of custom cable assemblies and wiring harnesses. At the closing, RF Industries, Ltd. paid the sellers \$3,100,000, which consisted of \$2,100,000 in cash, 50,467 shares of the Company's unregistered common stock valued at \$200,000 based on a per share price of \$3.96 (the volume weighted average price of the Company's common stock during the five trading days before the closing date) and, if certain financial targets are met by Rel-Tech over a three-year period, agreed to pay additional cash earn-out payments of up to \$800,000. Rel-Tech will operate as a stand-alone subsidiary for at least the next two years. Mr. Palumbo will serve as President of Rel-Tech at a base salary of \$150,000 per year. Mr. Palumbo will also be entitled to earn an annual bonus of up to 50% of his base salary. Rel-Tech has also entered into employment agreements to retain five key managers.

The acquisition was accounted for in accordance with the acquisition method of accounting. The acquired assets and assumed liabilities were recorded by the Company at their estimated fair values. The Company determined the estimated fair values with the assistance of appraisals or valuations performed by an independent third party specialist. Rel-Tech offers a full range of value-added services including product design, prototyping, stocking, bill of materials management, consignment and fulfillment programs. Rel-Tech provides engineered solutions to many leasing OEMs and markets its products to customers in commercial as well as military arenas. All assembly is performed at the Rel-Tech's facilities. These products and services supplement and enhance the existing markets of RF Industries without incurring substantially more costs than incurred in the purchase of Rel-Tech. These factors, among others, contributed to a purchase price in excess of the estimated fair value of Rel-Tech's net identifiable assets acquired and, as a result, we have recorded goodwill in connection with this acquisition. We do not expect the goodwill recorded to be deductible for income tax purposes.

Although the closing occurred on June 5, 2015, the acquisition of Rel-Tech is deemed to have become effective for financial accounting purposes as of June 1, 2015. Accordingly Rel-Tech's financial results have been included in the results of the Custom Cabling Manufacturing and Assembly segment as of June 1, 2015. The purchase price allocation is preliminary as it includes several estimates, which are being refined.

The following table summarizes the components of the estimated purchase price at fair value at June 1, 2015:

| | |
|--|-------------|
| Cash consideration paid | \$2,100,000 |
| RF Industries, Ltd. common shares issued (50,467 shares) | 200,000 |
| Earn-out | 610,000 |
| Total purchase price | \$2,910,000 |

The following table summarizes the preliminary allocation of the estimated purchase price at fair value at June 1, 2015:

| | |
|----------------------------------|-------------|
| Current assets | \$1,637,000 |
| Fixed assets | 68,000 |
| Other assets | 17,000 |
| Intangible assets | 1,425,000 |
| Goodwill | 833,000 |
| Deferred tax liabilities | (489,000) |
| Non-interest bearing liabilities | (581,000) |
| Net assets | \$2,910,000 |

The results of Rel-Tech's operations subsequent to June 1, 2015 have been included in the Company's consolidated results of operations. All costs related to the acquisition of Rel-Tech have been expensed as incurred. For the two month period ended July 31, 2015, Rel-Tech contributed \$1.2 million of revenue.

CompPro Product Line

On May 19, 2015, the Company purchased the CompPro braided product line ("CompPro"), including the intellectual property rights to that product line, for a total purchase price of \$700,000 cash. CompPro utilizes a patented compression technology that offers revolutionary advantages for a water-tight connection, easier installation, and improved system reliability on braided cables. CompPro is used by wireless network operators, installers and distributors in North America and other parts of the world. Included in the purchase is inventory, designs, intellectual property rights and to manufacture and sell CompPro products. Financial results for the CompPro products are

included in the results of the RF Connector and Cable Assembly segment beginning in the Company's fiscal quarter ending July 31, 2015.

The acquisition was accounted for in accordance with the acquisition method of accounting. The acquired assets were recorded by the Company at their estimated fair values. The Company determined the estimated fair values with the assistance of appraisals or valuations performed by an independent third party specialist. These above factors, among others, contributed to a purchase price in excess of the estimated fair value of CompPro's net identifiable assets acquired and, as a result, we have recorded goodwill in connection with this transaction.

Goodwill acquired was allocated to our operating segment and CompPro's reporting unit as part of the purchase price allocation. We expect the goodwill recorded to be deductible for income tax purposes. Acquired amortizable intangible assets are being amortized on a straight-line basis over their estimated useful lives ranging from three to seven years. The purchase price allocation is preliminary as the valuation being performed to record the business combination includes several estimates, which are being refined.

The following table summarizes the components of the estimated purchase price at fair value at May 19, 2015:

| | |
|-------------------------|-----------|
| Cash consideration paid | \$700,000 |
| Total purchase price | \$700,000 |

The following table summarizes the preliminary allocation of the estimated purchase price at fair value at May 19, 2015:

| | |
|-------------------|------------|
| Current assets | \$ 186,300 |
| Fixed assets | 67,500 |
| Intangible assets | 321,200 |
| Goodwill | 125,000 |
| Net assets | \$ 700,000 |

The results of CompPro's operations subsequent to May 19, 2015 have been included in the Company's consolidated results of operations. All costs related to the acquisition of CompPro have been expensed as incurred.

Comnet Telecom Supply, Inc.

The Company purchased 100% of the issued and outstanding shares of Comnet from Robert Portera, the sole shareholder of Comnet. Comnet is a New Jersey based manufacturer and supplier of telecommunications and data products, including fiber optic cables, cabling technologies, custom patch cord assemblies, data center consoles and other data center equipment. Comnet is a New York corporation that was formed in 1993. For income tax purposes, both parties have agreed to make an election under Internal Revenue Code 338(h) (10). At the closing, RF Industries, Ltd. paid Mr. Portera \$4,150,000 in cash and stock, and agreed to pay him up to an additional \$1,360,000 in cash as an earn-out over the next two years if Comnet meets certain financial milestones in the next two years. The purchase price paid at the closing consisted of \$3,090,000 in cash (of which \$300,000 has been deposited into a bank escrow account for one year as security for the seller's indemnification obligations under the stock purchase agreement) and 252,381 shares of RF Industries, Ltd.'s unregistered common stock, which shares were valued at \$1,060,000 based on a per share price of \$4.20 (the volume weighted average price of the common stock during the five trading days before the closing date). Comnet will be operated as a stand-alone subsidiary for at least the next two years. The Company entered into a two-year employment agreement with Mr. Portera pursuant to which Mr. Portera will be the President of Comnet and receive a base salary of \$210,000 per year. Mr. Portera will also be entitled to earn an annual bonus of up to 50% of his base salary. Since the acquisition of Comnet was effective for financial accounting purposes as of November 1, 2014 with an effective closing date of January 20, 2015, Comnet's financial results have been included in the results of the Custom Cabling Manufacturing and Assembly segment for the entire fiscal year ending October 31, 2015.

The acquisition was accounted for in accordance with the acquisition method of accounting. The acquired assets and assumed liabilities were recorded by the Company at their estimated fair values. The Company determined the estimated fair values with the assistance of appraisals or valuations performed by an independent third party specialist. The products manufactured and supplied by Comnet include fiber optic cables, cabling technologies, custom patch cord assemblies, data center consoles and other data center equipment. These products supplement and enhance the existing markets of RF Industries as well as tap into new data center markets that the Company would not have been

able to enter without incurring substantially more costs than incurred in the purchase of Comnet. The capital and other resources required to enhance the Company's fiber optics market and enter the data center market would have greatly exceeded the purchase price of \$4.15 million (excluding the potential earn-out). These factors, among others, contributed to a purchase price in excess of the estimated fair value of Comnet's net identifiable assets acquired and, as a result, we have recorded goodwill in connection with this transaction.

Goodwill acquired was allocated to our operating segment and Comnet reporting unit as part of the purchase price allocation. We expect the goodwill recorded to be deductible for income tax purposes. Acquired amortizable intangible assets are being amortized on a straight-line basis over their estimated useful lives ranging from three to eight years.

The following table summarizes the components of the estimated purchase price at fair value at November 1, 2014:

| | |
|---|-------------|
| Cash consideration paid | \$3,090,000 |
| RF Industries, Ltd. common shares issued (252,381 shares) | 1,060,000 |
| Earn-out | 1,235,000 |
| Total purchase price | \$5,385,000 |

The following table summarizes the final allocation of the purchase price at fair value at November 1, 2014: