

DYNAMIC MATERIALS CORP
Form 10-Q
July 29, 2014
Table of Contents

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 AND EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2014

OR

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES ACT OF 1934

FOR THE TRANSITION PERIOD FROM TO .

Commission file number 001-14775

DYNAMIC MATERIALS CORPORATION
(Exact name of Registrant as Specified in its Charter)

Delaware

(State of Incorporation or Organization)

5405 Spine Road, Boulder, Colorado 80301

(Address of principal executive offices, including zip code)

(303) 665-5700

(Registrant's telephone number, including area code)

84-0608431

(I.R.S. Employer Identification No.)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T 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.

Large accelerated filer

Accelerated filer

Edgar Filing: DYNAMIC MATERIALS CORP - Form 10-Q

Non-accelerated filer
(Do not check if smaller reporting company)

Smaller reporting company

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

The number of shares of Common Stock outstanding was 13,979,119 as of July 29, 2014.

Table of Contents

CAUTIONARY NOTE ABOUT FORWARD-LOOKING STATEMENTS

This quarterly report on Form 10-Q contains “forward-looking statements” within the meaning of section 27A of the Securities Act of 1933 and section 21E of the Securities Exchange Act of 1934. In particular, we direct your attention to Part I, Item 1- Condensed Consolidated Financial Statements; Item 2 - Management’s Discussion and Analysis of Financial Condition and Results of Operations; Item 3 - Quantitative and Qualitative Disclosures About Market Risk; and Part II, Item 1A — Risk Factors. We intend the forward-looking statements throughout this quarterly report on Form 10-Q and the information incorporated by reference herein to be covered by the safe harbor provisions for forward-looking statements. Statements contained in this report which are not historical facts are forward-looking statements that involve risks and uncertainties that could cause actual results to differ materially from projected results. All projections, guidance and other statements regarding our expected financial position and operating results, our business strategy, our financing plans and the outcome of any contingencies are forward-looking statements. These statements can sometimes be identified by our use of forward-looking words such as “may,” “believe,” “plan,” “anticipate,” “estimate,” “expect,” “intend,” and other phrases of similar meaning. The forward-looking information is based on information available as of the date of this quarterly report and on numerous assumptions and developments that are not within our control. Although we believe that our expectations as expressed in these forward-looking statements are reasonable, we cannot assure you that our expectations will turn out to be correct. Factors that could cause actual results to differ materially include, but are not limited to, the following: changes in global economic conditions; the ability to obtain new contracts at attractive prices; the size and timing of customer orders and shipment; our ability to realize sales from our backlog; fluctuations in customer demand; fluctuations in foreign currencies; competitive factors; the timely completion of contracts; the timing and size of expenditures; the timely receipt of government approvals and permits; the price and availability of metal and other raw material; the adequacy of local labor supplies at our facilities; current or future limits on manufacturing capacity at our various operations; our ability to successfully integrate acquired businesses; the availability and cost of funds; and general economic conditions, both domestic and foreign, impacting our business and the business of the end-market users we serve. Readers are cautioned not to place undue reliance on these forward-looking statements, which reflect management’s analysis only as of the date hereof. We undertake no obligation to publicly release the results of any revision to these forward-looking statements that may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events.

INDEX

	Page
<u>PART I - FINANCIAL INFORMATION</u>	
<u>Item 1</u>	<u>Condensed Consolidated Financial Statements</u> 4
	<u>Condensed Consolidated Balance Sheets as of June 30, 2014 (unaudited) and December 31, 2013</u> 4
	<u>Condensed Consolidated Statements of Operations for the three and six months ended June 30, 2014 and 2013 (unaudited)</u> 6
	<u>Condensed Consolidated Statements of Comprehensive Income for the three and six months ended June 30, 2014 and 2013 (unaudited)</u> 7
	<u>Condensed Consolidated Statement of Stockholders' Equity for the six months ended June 30, 2014 (unaudited)</u> 8
	<u>Condensed Consolidated Statements of Cash Flows for the six months ended June 30, 2014 and 2013 (unaudited)</u> 9
	<u>Notes to Condensed Consolidated Financial Statements (unaudited)</u> 10
<u>Item 2</u>	<u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> 16
<u>Item 3</u>	<u>Quantitative and Qualitative Disclosure about Market Risk</u> 24
<u>Item 4</u>	<u>Controls and Procedures</u> 24
<u>PART II - OTHER INFORMATION</u>	
<u>Item 1</u>	<u>Legal Proceedings</u> 26
<u>Item 1A</u>	<u>Risk Factors</u> 26
<u>Item 2</u>	<u>Unregistered Sales of Equity Securities and Use of Proceeds</u> 26
<u>Item 3</u>	<u>Defaults Upon Senior Securities</u> 26
<u>Item 4</u>	<u>Mine Safety Disclosures</u> 26
<u>Item 5</u>	<u>Other Information</u> 26
<u>Item 6</u>	<u>Exhibits</u> 26
	<u>Signatures</u> 27

Table of Contents

Part I - FINANCIAL INFORMATION

ITEM 1. Condensed Consolidated Financial Statements

DYNAMIC MATERIALS CORPORATION
 CONDENSED CONSOLIDATED BALANCE SHEETS
 (Amounts in Thousands, Except Share and Per Share Data)

	June 30, 2014 (unaudited)	December 31, 2013
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$8,692	\$10,617
Accounts receivable, net of allowance for doubtful accounts of \$504 and \$419, respectively	39,187	38,715
Inventory, net	46,335	41,550
Prepaid expenses and other	7,221	4,375
Current deferred tax assets	2,740	3,507
Total current assets	104,175	98,764
PROPERTY, PLANT AND EQUIPMENT	111,886	107,802
Less - accumulated depreciation	(46,990)	(42,787)
Property, plant and equipment, net	64,896	65,015
GOODWILL, net	37,161	37,970
PURCHASED INTANGIBLE ASSETS, net	32,939	36,458
DEFERRED TAX ASSETS	909	505
OTHER ASSETS, net	1,868	1,900
TOTAL ASSETS	\$241,948	\$240,612

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

Table of Contents

DYNAMIC MATERIALS CORPORATION
 CONDENSED CONSOLIDATED BALANCE SHEETS
 (Amounts in Thousands, Except Share and Per Share Data)

	June 30, 2014 (unaudited)	December 31, 2013
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	\$9,748	\$14,668
Accrued expenses	3,754	3,990
Dividend payable	559	550
Accrued income taxes	2,473	2,811
Accrued employee compensation and benefits	4,315	4,806
Customer advances	2,622	1,025
Current debt obligations	20	2,907
Current deferred tax liabilities	417	435
 Total current liabilities	 23,908	 31,192
 LINES OF CREDIT	 31,800	 26,400
 DEFERRED TAX LIABILITIES	 7,588	 8,347
 OTHER LONG-TERM LIABILITIES	 2,006	 1,881
 Total liabilities	 65,302	 67,820
 COMMITMENTS AND CONTINGENT LIABILITIES		
 STOCKHOLDERS' EQUITY:		
Preferred stock, \$0.05 par value; 4,000,000 shares authorized; no issued and outstanding shares	—	—
Common stock, \$0.05 par value; 25,000,000 shares authorized; 13,979,119 and 13,772,324 shares issued and outstanding, respectively	699	689
Additional paid-in capital	64,861	62,934
Retained earnings	116,808	113,399
Other cumulative comprehensive loss	(5,722	) (4,230)
 Total stockholders' equity	 176,646	 172,792
 TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	 \$241,948	 \$240,612

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

Table of Contents

DYNAMIC MATERIALS CORPORATION
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
 FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2014 AND 2013
 (Amounts in Thousands, Except Share and Per Share Data)
 (unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2014	2013	2014	2013
NET SALES	\$53,618	\$57,859	\$101,657	\$104,129
COST OF PRODUCTS SOLD	37,305	40,796	71,015	74,347
Gross profit	16,313	17,063	30,642	29,782
COSTS AND EXPENSES:				
General and administrative expenses	5,935	5,158	11,637	13,296
Selling and distribution expenses	4,770	4,324	9,018	8,375
Amortization of purchased intangible assets	1,617	1,568	3,232	3,153
Total costs and expenses	12,322	11,050	23,887	24,824
INCOME FROM OPERATIONS	3,991	6,013	6,755	4,958
OTHER INCOME (EXPENSE):				
Other income (expense), net	332	(420)	(103)	(124)
Interest expense	(174)	(183)	(283)	(355)
Interest income	1	1	5	4
INCOME BEFORE INCOME TAXES AND NON-CONTROLLING INTEREST	4,150	5,411	6,374	4,483
INCOME TAX PROVISION	1,263	1,956	1,849	785
NET INCOME	2,887	3,455	4,525	3,698
Less: Net income attributable to non-controlling interest	—	15	—	43
NET INCOME ATTRIBUTABLE TO DYNAMIC MATERIALS CORPORATION	\$2,887	\$3,440	\$4,525	\$3,655
INCOME PER SHARE:				
Basic	\$0.21	\$0.25	\$0.32	\$0.27
Diluted	\$0.21	\$0.25	\$0.32	\$0.27
WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING:				
Basic	13,672,457	13,526,623	13,668,223	13,523,028
Diluted	13,677,911	13,530,588	13,673,807	13,527,011
DIVIDENDS DECLARED PER COMMON SHARE	\$0.04	\$0.04	\$0.08	\$0.08

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

6

Table of Contents

DYNAMIC MATERIALS CORPORATION
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
 FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2014 AND 2013

(Amounts in Thousands)

(unaudited)

	Three months ended June 30,		Six months ended June 30,	
	2014	2013	2014	2013
Net income including non-controlling interest	\$2,887	\$3,455	\$4,525	\$3,698
Change in cumulative foreign currency translation adjustment	741	446	(1,492)	(3,181)
Total comprehensive income	3,628	3,901	3,033	517
Comprehensive income attributable to non-controlling interest	—	16	—	41
Comprehensive income attributable to Dynamic Materials Corporation	\$3,628	\$3,885	\$3,033	\$476

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

Table of Contents

DYNAMIC MATERIALS CORPORATION
 CONDENSED CONSOLIDATED STATEMENT OF STOCKHOLDERS' EQUITY
 FOR THE SIX MONTHS ENDED JUNE 30, 2014

(Amounts in Thousands)

(unaudited)

	Common Stock		Additional	Retained	Other	
	Shares	Amount	Paid-In	Earnings	Cumulative	Total
			Capital		Loss	
Balances, December 31, 2013	13,772,324	\$689	\$62,934	\$113,399	\$ (4,230)	\$172,792
Net income	—	—	—	4,525	—	4,525
Change in cumulative foreign currency translation adjustment	—	—	—	—	(1,492)	(1,492)
Shares issued in connection with stock compensation plans	206,795	10	224	—	—	234
Tax impact of stock-based compensation	—	—	112	—	—	112
Stock-based compensation	—	—	1,591	—	—	1,591
Dividends declared	—	—	—	(1,116)	—	(1,116)
Balances, June 30, 2014	13,979,119	\$699	\$64,861	\$116,808	\$ (5,722)	\$176,646

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

Table of Contents

DYNAMIC MATERIALS CORPORATION
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 FOR THE SIX MONTHS ENDED JUNE 30, 2014 AND 2013

(Amounts in Thousands)

(unaudited)

	2014	2013	
CASH FLOWS FROM OPERATING ACTIVITIES:			
Net income	\$4,525	\$3,698	
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation (including capital lease amortization)	3,922	2,874	
Amortization of purchased intangible assets	3,232	3,153	
Amortization of deferred debt issuance costs	51	51	
Stock-based compensation	1,591	2,057	
Deferred income tax provision (benefit)	(69)	) 196	
Gain on disposal of property, plant and equipment	5	21	
Change in:			
Accounts receivable, net	(706	) (5,012)
Inventory, net	(5,089	) 1,889	
Prepaid expenses and other	(2,876	) (543)
Accounts payable	(4,820	) 3,103	
Customer advances	1,612	3,427	
Accrued expenses and other liabilities	(687	) 484	
Net cash provided by operating activities	691	15,398	
CASH FLOWS FROM INVESTING ACTIVITIES:			
Acquisition of property, plant and equipment	(4,215	) (9,726)
Change in other non-current assets	(52	) 192	
Net cash used in investing activities	(4,267	) (9,534)
CASH FLOWS FROM FINANCING ACTIVITIES:			
Borrowings (repayments) on bank lines of credit, net	2,555	(9,811)
Payment on loans with former owners of LRI	(31	) (32)
Payment on capital lease obligations	(22	) (25)
Payment of dividends	(1,108	) (1,088)
Net proceeds from issuance of common stock to employees and directors	234	163	
Tax impact of stock-based compensation	112	(836)
Net cash provided by (used in) financing activities	1,740	(11,629)
EFFECTS OF EXCHANGE RATES ON CASH	(89	) (112)
NET DECREASE IN CASH AND CASH EQUIVALENTS	(1,925	) (5,877)
CASH AND CASH EQUIVALENTS, beginning of the period	10,617	8,200	
CASH AND CASH EQUIVALENTS, end of the period	\$8,692	\$2,323	

The accompanying notes are an integral part of these Condensed Consolidated Financial Statements.

9

Table of Contents

DYNAMIC MATERIALS CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Amounts in Thousands, Except Share and Per Share Data)
(unaudited)

1. BASIS OF PRESENTATION

The information included in the condensed consolidated financial statements is unaudited but includes all normal and recurring adjustments which, in the opinion of management, are necessary for a fair presentation of the interim periods presented. These condensed consolidated financial statements should be read in conjunction with the financial statements that are included in our Annual Report filed on Form 10-K for the year ended December 31, 2013.

2. SIGNIFICANT ACCOUNTING POLICIES

Principles of Consolidation

The condensed consolidated financial statements include the accounts of Dynamic Materials Corporation (“DMC”) and its controlled subsidiaries. Only subsidiaries in which controlling interests are maintained are consolidated. All significant intercompany accounts, profits, and transactions have been eliminated in consolidation.

Income Taxes

The effective tax rate for each of the periods reported differs from the U.S. statutory rate due primarily to favorable foreign permanent differences, variation in contribution to consolidated pre-tax income from each jurisdiction for the respective periods and differences between the U.S. and foreign tax rates (which range from 20% to 35%) on earnings that have been permanently reinvested.

In January 2013, the United States Congress authorized, and the President signed into law, legislation which retroactively changed federal tax laws for 2012. Since this legislation was enacted in 2013, the financial statement benefit from these changes, totaling \$914, was reflected in the provision for income taxes in the consolidated statement of operations during the six months ended June 30, 2013.

Earnings Per Share

Unvested awards of share-based payments with rights to receive dividends or dividend equivalents, such as our restricted stock awards (“RSAs”), are considered participating securities for purposes of calculating earnings per share (“EPS”) and require the use of the two class method for calculating EPS. Under this method, a portion of net income is allocated to these participating securities and therefore is excluded from the calculation of EPS allocated to common stock, as shown in the table below.

Table of Contents

Computation and reconciliation of earnings per common share are as follows:

	For the three months ended June 30, 2014			For the three months ended June 30, 2013		
	Income	Shares	EPS	Income	Shares	EPS
Basic earnings per share:						
Net income attributable to DMC	\$2,887			\$3,440		
Less income allocated to RSAs	(61	)		(53)	
Net income allocated to common stock for EPS calculation	\$2,826	13,672,457	\$0.21	\$3,387	13,526,623	\$0.25
Adjust shares for dilutives:						
Stock-based compensation plans		5,454			3,965	
Diluted earnings per share:						
Net income attributable to DMC	\$2,887			\$3,440		
Less income allocated to RSAs	(61	)		(53)	
Net income allocated to common stock for EPS calculation	\$2,826	13,677,911	\$0.21	\$3,387	13,530,588	\$0.25
	For the six months ended June 30, 2014			For the six months ended June 30, 2013		
	Income	Shares	EPS	Income	Shares	EPS
Basic earnings per share:						
Net income attributable to DMC	\$4,525			\$3,655		
Less income allocated to RSAs	(95	)		(56)	
Net income allocated to common stock for EPS calculation	\$4,430	13,668,223	\$0.32	\$3,599	13,523,028	\$0.27
Adjust shares for dilutives:						
Stock-based compensation plans		5,584			3,983	
Diluted earnings per share:						
Net income attributable to DMC	\$4,525			\$3,655		
Less income allocated to RSAs	(95	)		(56)	
Net income allocated to common stock for EPS calculation	\$4,430	13,673,807	\$0.32	\$3,599	13,527,011	\$0.27

Fair Value of Financial Instruments

The carrying value of cash and cash equivalents, trade accounts receivable and payable, accrued expenses, lines of credit and other debt approximate their fair value.

Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board issued an accounting standards update to clarify the principles of recognizing revenue and to develop a common revenue standard and disclosure requirements for U.S. GAAP and IFRS. The

Table of Contents

pronouncement is effective for reporting periods beginning after December 15, 2016. The adoption of this update is not expected to have a significant impact on our financial statements.

3. INVENTORIES

Inventories are stated at the lower-of-cost (first-in, first-out) or market value. Cost elements included in inventory are material, labor, subcontract costs, and manufacturing overhead. As necessary, we record provisions and maintain reserves for excess, slow moving and obsolete inventory. To determine reserve amounts, we regularly review inventory quantities on hand and values, and compare them to estimates of future product demand, market conditions, production requirements and technological developments.

Inventories consist of the following at June 30, 2014 and December 31, 2013 and include reserves of \$1,958 and \$1,729, respectively:

	June 30, 2014	December 31, 2013
Raw materials	\$ 15,503	\$ 13,122
Work-in-process	10,062	10,188
Finished goods	19,842	17,273
Supplies	928	967
	\$46,335	\$41,550

4. GOODWILL

The changes to the carrying amount of goodwill during the period are summarized below:

	NobelClad	Oilfield Products	Total
Goodwill balance at December 31, 2013	\$22,238	\$15,732	\$37,970
Adjustment due to recognition of tax benefit of tax amortization of certain goodwill	(179	) (306	) (485
Adjustment due to exchange rate differences	(186	) (138	) (324
Goodwill balance at June 30, 2014	\$21,873	\$15,288	\$37,161

5. PURCHASED INTANGIBLE ASSETS

The following table presents details of our purchased intangible assets, other than goodwill, as of June 30, 2014:

	Gross	Accumulated Amortization	Net
Core technology	\$23,189	\$(7,676	) \$15,513
Customer relationships	44,910	(28,145	) 16,765
Trademarks / Trade names	2,487	(1,826	) 661
Total intangible assets	\$70,586	\$(37,647	) \$32,939

Table of Contents

The following table presents details of our purchased intangible assets, other than goodwill, as of December 31, 2013:

	Gross	Accumulated Amortization	Net
Core technology	\$23,391	\$(7,155	) \$16,236
Customer relationships	45,269	(25,813	) 19,456
Trademarks / Trade names	2,510	(1,744	) 766
Total intangible assets	\$71,170	\$(34,712	) \$36,458

The change in the gross value of our purchased intangible assets from December 31, 2013 to June 30, 2014 was due to foreign currency translation.

6. CUSTOMER ADVANCES

On occasion, we require customers to make advance payments prior to the shipment of goods in order to help finance our inventory investment on large orders or to keep customers' credit limits at acceptable levels. As of June 30, 2014 and December 31, 2013, customer advances totaled \$2,622 and \$1,025, respectively, and originated from several customers.

7. DEBT

Lines of credit consisted of the following at June 30, 2014 and December 31, 2013:

	June 30, 2014	December 31, 2013
Syndicated credit agreement:		
U.S. Dollar revolving loan	\$31,800	\$26,400
German Bank line of credit	—	2,856
	31,800	29,256
Less current portion	—	(2,856)
Long-term lines of credit	\$31,800	\$26,400

Other debt consisted of the following at June 30, 2014 and December 31, 2013:

	June 30, 2014	December 31, 2013
Loans with former owners of LRI	\$20	\$51
Less current maturities	(20	) (51)
Other debt	\$—	\$—

Loan Covenants and Restrictions

Our existing loan agreements include various covenants and restrictions, certain of which relate to the payment of dividends or other distributions to stockholders; redemption of capital stock; incurrence of additional indebtedness; mortgaging, pledging or disposition of major assets; and maintenance of specified financial ratios. As of June 30, 2014, we were in compliance with all financial covenants and other provisions of our debt agreements.

Table of Contents

8. BUSINESS SEGMENTS

Our business is organized in the following two segments: NobelClad and Oilfield Products. The NobelClad segment uses explosives to perform metal cladding and shock synthesis of industrial diamonds. The most significant product of this group is clad metal which is used in the fabrication of pressure vessels, heat exchangers, and transition joints for various industries, including upstream oil and gas, oil refinery, petrochemicals, hydrometallurgy, aluminum production, shipbuilding, power generation, industrial refrigeration, and similar industries. The Oilfield Products segment manufactures, markets and sells oilfield perforating equipment and explosives, including detonating cords, detonators, bi-directional boosters and shaped charges, and seismic related explosives and accessories. Oilfield Products also utilizes a number of welding technologies to weld components for manufacturers of jet engine and ground-based turbines.

Prior to 2014, we were organized into three segments. At the beginning of 2014 management approved a change in operating structure whereby AMK Technical Services ("AMK") will operate within and be managed as part of the Oilfield Products business segment. Consequently, we combined AMK and DynaEnergetics into one reportable business segment, Oilfield Products. AMK represented 3% of segment assets, 4% of consolidated sales and 2% of segment operating income as of and for the year then ended December 31, 2013. All prior periods segment disclosures have been restated to conform to the 2014 presentation.

The accounting policies of all of the segments are the same as those described in the summary of significant accounting policies included herein and in our Annual Report on Form 10-K for the year ended December 31, 2013. Our reportable segments are separately managed strategic business units that offer different products and services. Each segment's products are marketed to different customer types and require different manufacturing processes and technologies.

Segment information is presented for the three and six months ended June 30, 2014 and 2013 as follows:

	Three months ended June 30,		Six months ended June 30,	
	2014	2013	2014	2013
Net sales:				
NobelClad	\$26,231	\$32,390	\$50,795	\$58,572
Oilfield Products	27,387	25,469	50,862	45,557
Consolidated net sales	\$53,618	\$57,859	\$101,657	\$104,129
	Three months ended June 30,		Six months ended June 30,	
	2014	2013	2014	2013
Income before income taxes:				
NobelClad	\$3,122	\$5,245	\$4,500	\$7,689
Oilfield Products	3,395	2,561	6,965	3,990
Segment operating income	6,517	7,806	11,465	11,679
Unallocated corporate expenses	(1,490	) (1,158	) (3,119	) (4,664
Stock-based compensation	(1,036	) (635	) (1,591	) (2,057
Other income (expense)	332	(420	) (103	) (124
Interest expense	(174	) (183	) (283	) (355
Interest income	1	1	5	4

Edgar Filing: DYNAMIC MATERIALS CORP - Form 10-Q

Consolidated income before income taxes	\$4,150	\$5,411	\$6,374	\$4,483
---	---------	---------	---------	---------

14

Table of Contents

	Three months ended June 30,		Six months ended June 30,	
	2014	2013	2014	2013
Depreciation and Amortization:				
NobelClad	\$1,682	\$1,467	\$3,414	\$2,923
Oilfield Products	1,862	1,558	3,740	3,104
Segment depreciation and amortization	\$3,544	\$3,025	\$7,154	\$6,027

During the three and six months ended June 30, 2014, no one customer accounted for more than 10% of total net sales. During the three months ended June 30, 2013, sales to one customer accounted for \$7,451 (12.9%) of total net sales. During the six months ended June 30, 2013, no one customer accounted for more than 10% of total net sales.

9. RETIREMENT EXPENSES

During the first quarter of 2013 and, as a result of board actions taken in January 2013, we recorded a one-time expense of \$2,965 associated with management retirements, the majority of which relates to the March 1, 2013 retirement of Yvon Cariou, our former President and Chief Executive Officer. This expense included \$894 of stock-based compensation, with the remainder representing cash payments.

Table of Contents

ITEM 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion should be read in conjunction with our historical consolidated financial statements and notes, as well as the selected historical consolidated financial data that are included in our Annual Report filed on Form 10-K for the year ended December 31, 2013.

Unless stated otherwise, all currency amounts in this discussion are presented in thousands (000's).

Executive Overview

Our business is organized into two segments: NobelClad and Oilfield Products. Prior to 2014, we were organized into three segments. At the beginning of 2014 management approved a change in operating structure whereby AMK Technical Services ("AMK") will operate within and be managed as part of the Oilfield Products business segment. Consequently, we combined AMK and DynaEnergetics into one reportable business segment, Oilfield Products. AMK represented 3% of segment assets, 4% of consolidated sales and 2% of segment operating income as of and for the year then ended December 31, 2013. All prior periods segment disclosures have been restated to conform to the 2014 presentation.

For the six months ended June 30, 2014, NobelClad accounted for 50% of our net sales and 39% of our income from operations before consideration of unallocated corporate expenses and stock-based compensation expense, which are not allocated to our business segments. Oilfield Products accounted for 50% and 61% of our first half 2014 sales and income from operations, respectively.

Our consolidated net sales for the six months ended June 30, 2014 decreased by \$2,472, or 2.4%, compared to the same period in 2013. Sales increased \$5,305 (11.6%) in our Oilfield Products segment and decreased \$7,777 (13.3%) in our NobelClad segment. Our consolidated income from operations increased to \$6,755 for the first half of 2014 compared to \$4,958 in the same period of 2013. The \$1,797 improvement in consolidated income from operations was due to a \$2,975 increase in Oilfield Products operating income and a \$2,011 decrease in aggregate unallocated corporate expenses and stock-based compensation, partially offset by a \$3,189 decline in NobelClad's operating income. The decrease in corporate expenses was driven by \$2,965 of non-recurring expenses in the first quarter of 2013 associated with management retirements. Consolidated operating income for the six months ended June 30, 2014 and 2013 includes amortization expense of \$3,232 and \$3,153, respectively. Net income was \$4,525 for the first half of 2014 compared to net income of \$3,655 for the same period of 2013.

Based upon the June 30, 2014 NobelClad backlog, recent quoting activity for this segment and sales trends in our Oilfield Products segment, we expect our full year 2014 consolidated net sales will be flat to up 4% from the \$209,573 reported in 2013.

Net sales

NobelClad's revenues are generated principally from sales of clad metal plates and sales of transition joints, which are made from clad plates, to customers that fabricate industrial equipment for various industries, including oil and gas, petrochemicals, alternative energy, hydrometallurgy, aluminum production, shipbuilding, power generation, industrial refrigeration, and similar industries. While a large portion of the demand for our clad metal products is driven by new plant construction and large plant expansion projects, maintenance and retrofit projects at existing chemical processing, petrochemical processing, oil refining, and aluminum smelting facilities also account for a significant portion of total demand. These industries tend to be cyclical in nature and timing of new order inflow remains difficult to predict; however, we believe that our NobelClad segment is well-positioned in the marketplace.

Oilfield Products' revenues are generated principally from the DynaEnergetics and AMK Technical Services' product lines. Dynaenergetics markets and sells shaped charges, detonators and detonating cord, and bidirectional boosters and perforating guns to customers who perform the perforation of oil and gas wells and from sales of seismic products to customers involved in oil and gas exploration activities. AMK Technical Services' revenues are generated from welding, heat treatment, and inspection services that are provided with respect to customer-supplied parts for customers primarily involved in the power generation industry and aircraft engine markets.

A significant portion of our revenue is derived from a relatively small number of customers; therefore, the failure to complete existing contracts on a timely basis, to receive payment for such services in a timely manner, or to enter into future contracts at projected volumes and profitability levels could adversely affect our ability to meet cash requirements exclusively through operating activities. We attempt to minimize the risk of losing customers or specific contracts by continually improving product quality, delivering product on time and competing aggressively on the basis of price.

Table of Contents

Gross profit and cost of products sold

Cost of of products sold for NobelClad includes the cost of metals and alloys used to manufacture clad metal plates, the cost of explosives, employee compensation and benefits, freight, outside processing costs, depreciation of manufacturing facilities and equipment, manufacturing supplies and other manufacturing overhead expenses.

Cost of products sold for Oilfield Products includes the cost of metals, explosives and other raw materials used to manufacture shaped charges, detonating products and perforating guns, welding wire and gas supplies as well as employee compensation and benefits, depreciation of manufacturing facilities and equipment, manufacturing supplies and other manufacturing overhead expenses.

NobelClad Backlog

We use backlog as a primary means to measure the immediate outlook for our NobelClad business. We define “backlog” at any given point in time as all firm, unfulfilled purchase orders and commitments at that time. Generally speaking, we expect to fill most backlog orders within the following 12 months. From experience, most firm purchase orders and commitments are realized. Our NobelClad backlog increased to \$40,056 at June 30, 2014 from \$36,930 at December 31, 2013.

Three and Six Months Ended June 30, 2014 Compared to the Three and Six Months Ended June 30, 2013

Net sales

	Three Months Ended			Percentage
	June 30, 2014	2013	Change		Change
Net sales	\$53,618	\$57,859	\$(4,241)	(7.3)%

	Six Months Ended			Percentage
	June 30, 2014	2013	Change	
Net sales	\$101,657	\$104,129	\$(2,472)	(2.4)%

Our consolidated net sales for the second quarter of 2014 decreased 7.3% to \$53,618 from \$57,859 for the second quarter of 2013. NobelClad sales decreased 19.0% to \$26,231 (49% of total sales) for the three months ended June 30, 2014 from \$32,390 (56% of total sales) for the same period of 2013. Since our NobelClad backlog of \$35,868 as of March 31, 2014 was significantly lower than the March 31, 2013 backlog of \$47,558, the \$6,159 decrease in second quarter 2014 sales relates to timing differences with respect to when orders enter our backlog and the subsequent shipment of these orders. Oilfield Products contributed \$27,387 (51% of total sales) to second quarter 2014 sales, an increase of 7.5% from sales of \$25,469 (44% of total sales) in the second quarter of 2013. The record quarter was due to improved product/customer mix including strong sales of DynaSelect, our fully integrated switch-detonator system introduced in the third quarter of 2013.

Our consolidated net sales for the first half of 2014 decreased 2.4% to \$101,657 from \$104,129 in the first half of 2013. NobelClad sales decreased 13.3% to \$50,795 for the six months ended June 30, 2014 (50% of total sales) from \$58,572 (56% of total sales) for the same period of 2013. The decrease in year-to-date Nobelclad sales relates primarily to the lower backlog and timing of shipments out of backlog. Oilfield Products contributed \$50,862 to first half 2014 sales (50% of total sales), which represents an increase of 11.6% from sales of \$45,557 for the first half of 2013 (44% of total sales). The increase in Oilfield products sales was driven by product/customer mix including the

DynaSelect system.

Gross profit

	Three Months Ended			Percentage	
	June 30, 2014	2013	Change	Change	
Gross profit	\$16,313	\$17,063	\$(750	) (4.4)%
Consolidated gross profit margin rate	30.4	% 29.5	%		

17

Table of Contents

	Six Months Ended			Percentage	
	June 30,		Change	Change	
	2014	2013			
Gross profit	\$30,642	\$29,782	\$860	2.9	%
Consolidated gross profit margin rate	30.1	% 28.6	%		

Our consolidated second quarter 2014 gross profit decreased by 4.4% to \$16,313 from \$17,063 for the three months ended June 30, 2013. Our second quarter 2014 consolidated gross profit margin rate increased to 30.4% from 29.5% in the second quarter of 2013. For the six months ended June 30, 2014, consolidated gross profit increased by 2.9% to \$30,642 from \$29,782 for the same period of 2013. Our year-to-date consolidated gross profit margin rate increased to 30.1% in 2014 from 28.6% in 2013.

NobelClad's gross profit margin decreased from 26.3% in the second quarter of 2013 to 25.0% in the second quarter of 2014. For the six-month period, our gross profit margin for this segment decreased to 22.2% in 2014 from 24.6% in 2013. The decrease in both our second quarter and year-to-date gross margin rate relates principally to lower sales volume and higher manufacturing overhead expenses compared to the same periods in 2013. The increase in manufacturing overhead expenses primarily was attributable to lower fixed cost absorption from lower sales volume. As has been the case historically, we expect to see continued fluctuations in NobelClad's quarterly gross margin rates in the future that result from fluctuations in quarterly sales volume and product/customer mix.

Oilfield Products' gross profit margin increased to 35.9% in the second quarter of 2014 from 33.9% in the second quarter of 2013. Oilfield Products reported a gross profit margin of 38.3% for the first half of 2014 compared to a gross profit margin of 34.0% for the first half of 2013. The improved gross margin performance relates principally to favorable product/customer mix including sales of our higher margin DynaSelect system.

Based upon the expected contribution to 2014 consolidated net sales by each of our two business segments, we expect our consolidated full year 2014 gross margin to be in a range of 29% to 30%.

General and administrative expenses

	Three Months Ended			Percentage	
	June 30,		Change	Change	
	2014	2013			
General and administrative expenses	\$5,935	\$5,158	\$777	15.1	%
Percentage of net sales	11.1	% 8.9	%		

	Six Months Ended			Percentage	
	June 30,		Change	Change	
	2014	2013			
General and administrative expenses	\$11,637	\$13,296	\$(1,659)	(12.5))%
Percentage of net sales	11.4	% 12.8	%		

General and administrative expenses increased by \$777, or 15.1%, to \$5,935 for the three months ended June 30, 2014 from \$5,158 for the same period of 2013. This increase was driven by an increase of \$356 in stock-based compensation expense and a \$259 aggregate increase in salaries, benefits and payroll taxes. As a percentage of net sales, general and administrative expenses increased to 11.1% in the second quarter of 2014 from 8.9% in the second quarter of 2013.

General and administrative expenses decreased by 12.5% to \$11,637 for the six months ended June 30, 2014 from \$13,296 for the same period of 2013. Excluding the \$2,965 impact in 2013 from non-recurring expenses associated with management retirements, our general and administrative expenses increased \$1,306 or 12.6% from a \$424 aggregate increase in salaries, benefits and payroll taxes, an increase of \$381 in stock-based compensation expense and a \$319 increase in professional services. The increases were driven by year-over-year headcount additions to support business development initiatives, corporate branding and recruiting expenses. Excluding the impact of non-recurring executive management retirement expenses in 2013, general and administrative expenses, as a percentage of net sales, increased to 11.4% for the first half 2014 from 9.9% for the first half of 2013.

Table of Contents

Selling and distribution expenses

	Three Months Ended			Percentage	
	June 30,				
	2014	2013	Change	Change	
Selling and distribution expenses	\$4,770	\$4,324	\$446	10.3	%
Percentage of net sales	8.9	% 7.5	%		

	Six Months Ended			Percentage	
	June 30,				
	2014	2013	Change	Change	
Selling and distribution expenses	\$9,018	\$8,375	\$643	7.7	%
Percentage of net sales	8.9	% 8.0	%		

Our selling and distribution expenses increased by 10.3% to \$4,770 in the second quarter of 2014 from \$4,324 in the second quarter of 2013. The increase was primarily due to higher commission expense of \$175, a \$66 aggregate increase in salaries, benefits and payroll taxes and an increase of \$40 in stock-based compensation expense. As a percentage of net sales, selling and distribution expenses increased to 8.9% in the second quarter of 2014 from 7.5% in the second quarter of 2013.

Our selling and distribution expenses increased by 7.7% to \$9,018 for the first half of 2014 from \$8,375 for the first half of 2013. The increase was primarily due to higher commission expense of \$260, a \$136 aggregate increase in salaries, benefits and payroll taxes and an increase of \$51 in stock-based compensation expense. As a percentage of net sales, selling and distribution expense increased to 8.9% for the first half of 2014 from 8.0% for the first half of 2013.

Our consolidated selling and distribution expenses for the three months ended June 30, 2014 include \$1,620 and \$3,060, respectively, for our NobelClad and Oilfield Products business segments as compared to \$1,365 and \$2,910, respectively, for the second quarter of 2013. Our consolidated selling and distribution expenses for the six months ended June 30, 2014 include \$3,269 and \$5,612, respectively, for our NobelClad and Oilfield Products business segments as compared to \$2,969 and \$5,319, respectively, for the first half of 2013. The higher level of selling and distribution expenses for our Oilfield Products segment relative to its contribution to our consolidated net sales reflects the need, particularly in North America, to maintain a number of strategically located distribution centers that are in close proximity to areas which contain a large concentration of oilfields and enjoy a high volume of related oil and gas drilling activities.

Amortization expense

	Three Months Ended			Percentage	
	June 30,				
	2014	2013	Change	Change	
Amortization of purchased intangible assets	\$1,617	\$1,568	\$49	3.1	%
Percentage of net sales	3.0	% 2.7	%		

	Six Months Ended			Percentage	
	June 30,				
	2014	2013	Change	Change	
Amortization of purchased intangible assets	\$3,232	\$3,153	\$79	2.5	%
Percentage of net sales	3.2	% 3.0	%		

Amortization expense relates to intangible assets in connection with acquisitions in our Oilfield Products segment. The \$49 increase in second quarter 2014 amortization expenses reflects the impact of foreign currency translation. Amortization expense for the three months ended June 30, 2014 includes \$1,275, \$293, and \$49 relating to values assigned to customer relationships, core technology, and trademarks/trade names, respectively. Amortization expense for the three months ended June 30, 2013 includes \$1,242, \$279 and \$47 relating to values assigned to customer relationships, core technology, and trademarks/trade names, respectively.

Amortization expense for the six months ended June 30, 2014 includes \$2,549, \$585, and \$98 relating to values assigned to customer relationships, core technology, and trademarks/trade names, respectively. Amortization for the six months ended June

Table of Contents

30, 2013 includes \$2,497, \$562, and \$94 relating to values assigned to customer relationships, core technology, and trademarks/trade names, respectively.

Amortization expense (as measured in Euros) associated with the DYNAenergetics acquisition and the acquisition of the two Russian joint ventures is expected to approximate €3,333 and €225, respectively, in 2014. Our 2014 amortization expense associated with the Austin Explosives and TRX Industries acquisitions is expected to approximate \$435 and \$895, respectively, and our 2014 amortization expense (as measured in Canadian dollars) associated with the LRI acquisition is expected to approximate 80 CAD.

Operating income

	Three Months Ended			Percentage	
	June 30, 2014	2013	Change	Change	
Operating income	\$3,991	\$6,013	\$(2,022)	(33.6))%
	Six Months Ended			Percentage	
	June 30, 2014	2013	Change	Change	
Operating income	\$6,755	\$4,958	\$1,797	36.2	%

Our consolidated operating income decreased by \$2,022 to \$3,991 in the second quarter of 2014 from \$6,013 in the second quarter of 2013. These operating income totals for the second quarters of 2014 and 2013 include \$1,490 and \$1,158, respectively, of unallocated corporate expenses and \$1,036 and \$635, respectively, of stock-based compensation expense. Our consolidated operating income increased by \$1,797 to \$6,755 for the first half of 2014 from \$4,958 for the first half of 2013. These operating income totals for 2014 and 2013 include \$3,119 and \$4,664, respectively, of unallocated corporate expenses and \$1,591 and \$2,057, respectively, of stock-based compensation expense. These expenses are not allocated to our business segments and thus are not included in the below 2014 and 2013 operating income totals for NobelClad and Oilfield Products.

The increase in our consolidated operating income for the first half of 2014 reflects decreases in stock-based compensation expense and unallocated corporate expenses of \$466 and \$1,545, respectively and a decrease of \$214 in the aggregate operating income reported by our two business segments. The aggregate net decrease of \$2,011 in unallocated corporate expenses and stock-based compensation expense primarily relates to the \$2,965 of non-recurring expenses in the first quarter 2013 associated with management retirements.

NobelClad's operating income of \$3,122 in the second quarter of 2014 decreased 40.5% from \$5,245 in the second quarter of 2013. Operating results of NobelClad for the three months ended June 30, 2014 and 2013 include \$548 and \$521, respectively, of amortization expense of purchased intangible assets. NobelClad reported operating income of \$4,500 in the first half of 2014 compared to \$7,689 in the first half of 2013. Operating results of NobelClad for the six months ended June 30, 2014 and 2013 include \$1,095 and \$1,049, respectively, of amortization expense of purchased intangible assets. The decrease in operating income for the quarter and year-to-date periods was attributable to lower sales combined with the higher manufacturing overhead expenses discussed above.

Oilfield Products' operating income of \$3,395 in the second quarter of 2014 increased 32.6% from \$2,561 in the second quarter of 2013. Oilfield Products' operating results for the three months ended June 30, 2014 and 2013 include \$1,069 and \$1,047, respectively, of amortization expense of purchased intangible assets. Oilfield Products reported operating income of \$6,965 in the first half of 2014 compared to \$3,990 in the first half of 2013. Operating results of Oilfield Products for the six months ended June 30, 2014 and 2013 include \$2,137 and \$2,104, respectively,

Edgar Filing: DYNAMIC MATERIALS CORP - Form 10-Q

of amortization expense of purchased intangible assets. The increase in operating income for the quarter and year-to-date periods was largely attributable to the improved sales volumes and gross margin percentages as discussed above.

Other income (expense), net	Three Months Ended			Percentage	
	June 30, 2014	2013	Change	Change	
Other income (expense), net	\$332	\$(420)	) \$752	(179.0)%

20

Table of Contents

	Six Months Ended			Percentage Change	
	June 30, 2014	2013	Change		
Other income (expense), net	\$(103) \$(124) \$21	(16.9)%

Net other income was \$332 in the second quarter of 2014 compared to net other expense of \$420 in the second quarter of 2013. Our second quarter 2014 net other income of \$332 included net realized and unrealized foreign exchange gains of \$270. Our second quarter 2013 net other expense of \$420 included net realized and unrealized foreign exchange losses of \$456.

Net other expense was \$103 for the six month ended June 30, 2014 compared to net other expense of \$124 for the same period of 2013. Our first half 2014 net other expense of \$103 included net realized and unrealized foreign exchange losses of \$178. Our first half 2013 net other expense of \$124 includes net realized and unrealized foreign exchange losses of \$136.

	Three Months Ended			Percentage Change	
	June 30, 2014	2013	Change		
Interest income (expense), net	\$(173) \$(182) \$9	(4.9)%

	Six Months Ended			Percentage Change	
	June 30, 2014	2013	Change		
Interest income (expense), net	\$(278) \$(351) \$73	(20.8)%

Net interest expense was \$173 in the second quarter of 2014 compared to net interest expense of \$182 in the second quarter of 2013. Net interest expense was \$278 for the first half of 2014 compared to net interest expense of \$351 for the first half of 2013. The small decrease reflects lower average outstanding borrowings in the first quarter of 2014 as interest rates remained relatively stable.

	Three Months Ended			Percentage Change	
	June 30, 2014	2013	Change		
Income tax provision	\$1,263	\$1,956	\$(693	) (35.4)%
Effective tax rate	30.4	% 36.1	%		

	Six Months Ended			Percentage Change	
	June 30, 2014	2013	Change		
Income tax provision	\$1,849	\$785	\$1,064	135.5	%
Effective tax rate	29.0	% 17.5	%		

The effective tax rate decreased to 30.4% for the second quarter of 2014 compared to 36.1% for the second quarter of 2013. We recorded an income tax provision of \$1,263 in the second quarter of 2014 compared to an income tax provision of \$1,956 in the second quarter of 2013. Our consolidated income tax provision for the three months ended

June 30, 2014 and 2013 included a U.S. tax benefit of \$48 in 2014 and a U.S. tax provision of \$1,240 in 2013, with the remainder relating to net foreign tax provisions of \$1,311 and \$716, respectively, associated with our foreign operations and holding companies.

The effective tax rate increased to 29.0% for the first half of 2014 compared to 17.5% for the first half of 2013. Excluding the effects of the \$914 tax benefit we recorded in the first quarter 2013 and \$404 of additional tax expense we recorded in the second quarter 2013, our first half 2013 effective tax rate would have been 28.8%. For the six months ended June 30, 2014, we recorded an income tax provision of \$1,849 compared to an income tax provision of \$785 for the same period of 2013. Our

Table of Contents

consolidated income tax provision for the six months ended June 30, 2014 and 2013 included \$776 and \$766, respectively, related to U.S. tax benefit, with the remainder relating to net foreign tax provisions of \$2,625 and \$1,551, respectively.

In January 2013, the United States Congress authorized, and the President signed into law, changes to the U. S. income tax laws which were retroactive to January 1, 2012. However, since these changes were enacted in 2013, the financial statement benefit of such legislation could not be reflected until the first quarter of 2013. The \$914 tax benefit that we recognized in the first quarter of 2013 had a significant favorable impact on our first quarter and first half of 2013 effective tax rate. During the second quarter of 2013, we recorded a one-time tax expense of \$404 associated with a German tax audit settlement. This non-recurring adjustment had a significant unfavorable impact on our second quarter and first half 2013 effective tax rate.

Our statutory income tax rates range from 20% to 35% for our various U.S. and foreign operating entities and holding companies. Fluctuations in our consolidated effective tax rate also reflect the different tax rates in our U.S. and foreign tax jurisdictions and the variation in contribution to consolidated pre-tax income from each jurisdiction for the respective year.

We expect our blended effective tax rate for the full year 2014 to range from 29% to 30% based on projected pre-tax income.

Adjusted EBITDA

	Three Months Ended			Percentage	
	June 30, 2014	2013	Change	Change	
Adjusted EBITDA	\$8,571	\$9,658	\$(1,087)	(11.3))%
	Six Months Ended			Percentage	
	June 30, 2014	2013	Change	Change	
Adjusted EBITDA	\$15,500	\$12,999	\$2,501	19.2	%

Adjusted EBITDA is a non-GAAP measure that we believe provides an important indicator of our ongoing operating performance. Our aggregate non-cash depreciation, amortization of purchased intangible assets and stock-based compensation expense for the three months ended June 30, 2014 and 2013 was \$4,580 and \$3,660, respectively, and for the six months ended June 30, 2014 and 2013 was \$8,745 and \$8,084, respectively. These aggregate non-cash charges represent a significant percentage of the consolidated operating income that we reported for these periods. We use non-GAAP EBITDA and Adjusted EBITDA in our operational and financial decision-making and believe that these non-GAAP measures facilitate a more meaningful and accurate comparison of the operating performance of our two business segments than do certain GAAP measures. Research analysts, investment bankers and lenders also use EBITDA and Adjusted EBITDA to assess operating performance. In addition, during 2014, our management incentive awards will be based, in part, upon the amount of EBITDA achieved during the year. A portion of the equity incentive awards granted in 2014 to our named executive officers will be earned based on the amount of Adjusted EBITDA achieved in 2014 and 2015. The following is a reconciliation of the most directly comparable GAAP measure to Adjusted EBITDA.

	Three Months Ended		Six Months Ended	
	June 30, 2014	2013	June 30, 2014	2013
Net income attributable to DMC	\$2,887	\$3,440	\$4,525	\$3,655

Edgar Filing: DYNAMIC MATERIALS CORP - Form 10-Q

Interest expense	174	183	283	355
Interest income	(1	) (1	) (5	) (4
Provision for income taxes	1,263	1,956	1,849	785
Depreciation	1,927	1,457	3,922	2,874
Amortization of purchased intangible assets	1,617	1,568	3,232	3,153
EBITDA	7,867	8,603	13,806	10,818
Stock-based compensation	1,036	635	1,591	2,057
Other (income) expense, net	(332	) 420	103	124
Adjusted EBITDA	\$8,571	\$9,658	\$15,500	\$12,999

Table of Contents

Adjusted EBITDA decreased by 11.3% to \$8,571 in the second quarter of 2014 from \$9,658 in the second quarter of 2013 primarily due to the \$2,022 decrease in second quarter 2014 operating income. Adjusted EBITDA increased by 19.2% to \$15,500 for the first half of 2014 from \$12,999 for the first half of 2013 primarily due to the increase in operating income.

Liquidity and Capital Resources

We have historically financed our operations and business acquisitions from a combination of internally generated cash flow, revolving credit borrowings, various long-term debt arrangements, and the issuance of common stock. We believe that cash flow from operations and funds available under our current credit facilities and any future replacement thereof will be sufficient to fund the working capital, debt service, and capital expenditure requirements of our current business operations for the foreseeable future. Nevertheless, our ability to generate sufficient cash flows from operations will depend upon our success in executing our strategies. If we are unable to (i) realize sales from our backlog; (ii) secure new customer orders; (iii) continue selling products at attractive margins; and (iv) continue to implement cost-effective internal processes, our ability to meet cash requirements through operating activities could be impacted. Furthermore, any restriction on the availability of borrowings under our credit facilities could negatively affect our ability to meet future cash requirements.

Debt facilities

On December 21, 2011, we entered into a five-year syndicated credit agreement, which provides revolving loan availability of \$36,000, 16,000 Euros and 1,500 Canadian Dollars through a syndicate of four banks, and amends and restates in its entirety our prior syndicated credit agreement entered into on November 16, 2007. We also maintain a line of credit with a German bank for certain DYNAenergetics operations. This line of credit provides a borrowing capacity of 4,000 Euros.

As of June 30, 2014, U.S. dollar revolving loans of \$31,800 were outstanding under our syndicated credit agreement and \$20 was outstanding under loan agreements with the former owners of LRI. While we had approximately \$31,525 of unutilized revolving credit loan capacity as of June 30, 2014 under our various credit facilities, future borrowings are subject to compliance with financial covenants that could significantly limit availability.

There are two significant financial covenants under our syndicated credit agreement, the leverage ratio and fixed charge coverage ratio requirements. The leverage ratio is defined in the credit agreement as Consolidated Funded Indebtedness at the balance sheet date as compared to Consolidated EBITDA, which is defined as earnings before provisions for income taxes, interest expense, depreciation and amortization, extraordinary, non-recurring charges and other non-cash charges, for the previous twelve months. For the six months ended June 30, 2014 and the year ended December 31, 2013, Consolidated EBITDA approximated the "Adjusted EBITDA" that we reported for the respective periods. As of June 30, 2014, the maximum leverage ratio permitted by our credit facility was 2.0 to 1.0. The actual leverage ratio as of June 30, 2014 was 1.06 to 1.0. The maximum leverage ratio permitted as of September 30 and December 31, 2014 is 2.0 to 1.0.

The fixed charge ratio, as defined in the credit agreement, means, for any period, the ratio of Consolidated EBITDA to Fixed Charges. Consolidated EBITDA is defined above and Fixed Charges equals the sum of cash interest expense, cash dividends, cash income taxes and an amount equal to 75% of depreciation expense. For the trailing twelve months ended June 30, 2014, the minimum fixed charge ratio permitted by our credit facility was 2.0 to 1.0. The actual fixed charge ratio for the trailing twelve months ended June 30, 2014 was 2.35 to 1.0. The minimum fixed charge coverage ratio permitted for the twelve month periods ending September 30 and December 31, 2014 is 2.0 to 1.0.

Debt and other contractual obligations and commitments

Our existing loan agreements include various covenants and restrictions, certain of which relate to the payment of dividends or other distributions to stockholders, redemption of capital stock, incurrence of additional indebtedness, mortgaging, pledging or disposition of major assets, and maintenance of specified financial ratios. As of June 30, 2014, we were in compliance with all financial covenants and other provisions of our debt agreements.

Our principal cash flows related to debt obligations and other contractual obligations and commitments have not materially changed since December 31, 2013.

Cash flows from operating activities

Net cash provided by operating activities was \$691 for the six months ended June 30, 2014 compared with \$15,398 for the same period in 2013. The year-over-year decline of \$14,707 was driven by a \$15,914 net increase in working capital, which more than offset higher net income of \$827. We experienced negative net working capital changes of \$12,566 in the first first half of

Table of Contents

2014 compared to net positive changes in working capital of \$3,348 in the same period of 2013. Negative changes in our 2014 working capital included an increase in inventories and prepaid expenses of \$5,089 and \$2,876, respectively, and a decrease of \$4,820 in accounts payable. The increases in working capital were driven by a short-term inventory build in DynaEnergetics related to customer order patterns and ramp up of the new DynaSelect system introduction, timing of accounts payable and prepayment for raw materials with long lead times but favorable pricing. These negative changes were partly offset by a \$1,612 increase in customer advances.

Net cash flows provided by operating activities increased to \$15,398 in the first half of 2013 from \$8,075 in the first half 2012, reflecting a \$1,390 decrease in net income that was offset by positive changes in net working capital of \$7,694 and positive changes in non-cash adjustments aggregating \$1,019. We experienced net positive changes in working capital of \$3,348 in the first half of 2013 compared to net negative changes in working capital of \$4,346 in the same period of 2012. Positive changes in our 2013 working capital included a decrease in inventories of \$1,889 and increases of \$3,103, \$3,427 and \$484 in accounts payable, customer advances, and accrued expenses and other liabilities, respectively. These positive changes were partly offset by an increase of \$5,012 in accounts receivable and an increase of \$543 in prepaid expenses and other. All of foregoing changes in working capital related to typical fluctuations in our business flow and the related timing of cash payments and receipts.

Cash flows from investing activities

Net cash flows used in investing activities for the six months ended June 30, 2014 totaled \$4,267 and consisted almost entirely of capital expenditures, which included \$2,552 for our green field investment in Russia to expand capacity in DynaEnergetics.

Net cash flows used in investing activities for the first half of 2013 totaled \$9,534 and consisted almost entirely of capital expenditures. Our capital expenditures included \$5,626 for our greenfield projects in Russia and North America.

Cash flows from financing activities

Net cash flows provided by financing activities for the first half of 2014 totaled \$1,740, which included net borrowings on bank lines of credit of \$2,555 which was partially offset by payment of quarterly dividends of \$1,108.

Net cash flows used in financing activities for the first half of 2013 totaled \$11,629, which included net repayments on bank lines of credit of \$9,811 and payment of quarterly dividends of \$1,088.

Payment of Dividends

On May 14, 2014, our board of directors declared a quarterly cash dividend of \$0.04 per share which was paid on July 15, 2014. The dividend totaled \$559 and was payable to shareholders of record as of June 30, 2014. We also paid a quarterly cash dividend of \$0.04 per share in the first quarter of 2014 and the first and second quarters of 2013.

We may continue to pay quarterly dividends in the future subject to capital availability and periodic determinations that cash dividends are in compliance with our debt covenants and are in the best interests of our stockholders, but we cannot assure you that such payments will continue. Future dividends may be affected by, among other items, our views on potential future capital requirements, future business prospects, debt covenant compliance, changes in federal income tax laws, or any other factors that our board of directors deems relevant. Any decision to pay cash dividends is and will continue to be at the discretion of board of directors.

Critical Accounting Policies

Our critical accounting policies have not changed from those reported in our Annual Report filed on Form 10-K for the year ended December 31, 2013.

ITEM 3. Quantitative and Qualitative Disclosure about Market Risk

There have been no events that materially affect our quantitative and qualitative disclosure about market risk from that reported in our Annual Report on Form 10-K for the year ended December 31, 2013.

ITEM 4. Controls and Procedures

We maintain disclosure controls and procedures that are designed to ensure that information required to be disclosed in our Exchange Act reports is accurately recorded, processed, summarized and reported within the time periods specified in the SEC's

Table of Contents

rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating the disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily applied its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

As of June 30, 2014, we carried out an evaluation, under the supervision and with the participation of our management, including our Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e)). Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective at the reasonable assurance level. There have been no changes in our internal controls during the quarter ended June 30, 2014 or in other factors that could materially affect our internal controls over financial reporting.

Our management, including our Chief Executive Officer and Chief Financial Officer, does not expect that our disclosure controls or our internal controls will prevent all errors and all fraud. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. As a result of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within our company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple errors or mistakes. As a result of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected. Accordingly, our disclosure controls and procedures are designed to provide reasonable, not absolute, assurance that the disclosure controls and procedures are met.

Table of Contents

Part II - OTHER INFORMATION

Item 1. Legal Proceedings

None.

Item 1A. Risk Factors

There have been no significant changes in the risk factors identified as being attendant to our business in our Annual Report on Form 10-K for the year ended December 31, 2013.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Mine Safety Disclosures

Not applicable.

Item 5. Other Information

None.

Item 6.

Exhibits

3.1 Certificate of Incorporation of the Company, as amended.

31.1 Certification of the President and Chief Executive Officer pursuant to 17 CFR 240.13a-14(a) or 17 CFR 240.15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

31.2 Certification of the Senior Vice President and Chief Financial Officer pursuant to 17 CFR 240.13a-14(a) or 17 CFR 240.15d-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of the President and Chief Executive Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

32.2 Certification of the Senior Vice President and Chief Financial Officer pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

101 The following materials from the Quarterly Report on Form 10-Q of Dynamic Materials Corporation, for the quarter ended June 30, 2014, formatted in XBRL (eXtensible Business Reporting Language): (i) the Condensed Consolidated Balance Sheets, (ii) the Condensed Consolidated Statements of Operations, (iii) the Condensed

Consolidated Statement of Stockholders' Equity, (iv) the Condensed Consolidated Statements of Cash Flows, and (v) the Notes to Condensed Consolidated Financial Statements, tagged as blocks of text.*

* Pursuant to Rule 406T of Regulation S-T, the Interactive Data Files on Exhibit 101 hereto are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933, as amended, are deemed not filed for purposes of Section 18 of the Securities and Exchange Act of 1934, as amended, and otherwise are not subject to liability under those sections.

26

Table of Contents

SIGNATURES

In accordance with 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.

DYNAMIC MATERIALS CORPORATION
(Registrant)

Date: July 29, 2014

/s/ Michael Kuta
Michael Kuta, Chief Financial Officer (Duly
Authorized Officer and Principal Financial and
Accounting Officer)