

BALLANTYNE STRONG, INC.
Form 10-Q
August 09, 2013

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 30, 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 Number: 1-13906

BALLANTYNE STRONG, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware

(State or Other Jurisdiction of
Incorporation or Organization)

47-0587703

(IRS Employer
Identification Number)

13710 FNB Parkway, Suite 400, Omaha, Nebraska

(Address of Principal Executive Offices)

68154

(Zip Code)

(402) 453-4444

(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 twelve 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 (§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 definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act (check one):

Large accelerated filer

Accelerated filer

Non-accelerated filer

Smaller reporting company

(Do not check if a smaller reporting company)

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

Yes No

Indicate the number of shares outstanding of each of the issuer's classes of common stock as of the latest practicable date:

Class	Outstanding as of August 1, 2013
Common Stock, \$.01, par value	14,138,297 shares

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PART I. Financial Information**Item 1. Condensed Consolidated Financial Statements****Ballantyne Strong, Inc. and Subsidiaries****Condensed Consolidated Balance Sheets****(In thousands)**

	June 30, 2013	December 31, 2012
	(Unaudited)	
Assets		
Current assets:		
Cash and cash equivalents	\$ 45,121	\$ 40,168
Accounts receivable (net of allowance for doubtful accounts of \$592 and \$487, respectively)	13,379	26,227
Inventories:		
Finished goods, net	8,565	6,706
Work in process	1,053	1,018
Raw materials and components, net	3,640	3,247
Total inventories, net	13,258	10,971
Other current assets	4,595	6,741
Total current assets	76,353	84,107
Property, plant and equipment (net of accumulated depreciation of \$4,235 and \$3,750, respectively)	10,264	11,105
Note receivable	2,232	2,232
Other assets	2,277	2,102
Total assets	\$ 91,126	\$ 99,546
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$ 8,882	\$ 16,646
Accrued expenses	4,558	5,313
Customer deposits/deferred revenue	4,348	5,251
Total current liabilities	17,788	27,210
Deferred revenue	2,936	3,302
Deferred income taxes	646	580
Other accrued expenses, net of current portion	1,830	1,538
Total liabilities	23,200	32,630
Stockholders' equity:		

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Preferred stock, par value \$.01 per share; Authorized 1,000 shares, none outstanding	—	—
Common stock, par value \$.01 per share; Authorized 25,000 shares; issued 16,869 and 16,782 shares at June 30, 2013 and December 31, 2012, respectively; 14,138 and 14,051 shares outstanding at June 30, 2013 and December 31, 2012, respectively	167	167
Additional paid-in capital	37,988	37,770
Accumulated other comprehensive income:		
Foreign currency translation	(822) 269
Postretirement benefit obligations	46	46
Retained earnings	48,786	46,903
	86,165	85,155
Less 2,731 of common shares in treasury, at cost at June 30, 2013 and December 31, 2012	(18,239) (18,239)
Total stockholders' equity	67,926	66,916
Total liabilities and stockholders' equity	\$ 91,126	\$ 99,546

See accompanying notes to condensed consolidated financial statements.

Ballantyne Strong, Inc. and Subsidiaries Condensed Consolidated Statements of Operations**Three and Six Months Ended June 30, 2013 and 2012****(In thousands, except per share data)****(Unaudited)**

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Net revenues	\$24,395	\$46,708	\$52,016	\$90,727
Cost of revenues	19,715	40,350	43,423	78,030
Gross profit	4,680	6,358	8,593	12,697
Selling and administrative expenses:				
Selling	870	1,229	1,736	2,056
Administrative	2,453	3,135	4,954	6,202
Total selling and administrative expenses	3,323	4,364	6,690	8,258
Gain (loss) on the sale/disposal/transfer of assets	3	460	4	1,378
Income from operations	1,360	2,454	1,907	5,817
Net interest income (expense)	1	(11)	16	(22)
Equity income of joint venture	(12)	(25)	(118)	66
Other income, net	247	253	496	413
Income before income taxes	1,596	2,671	2,301	6,274
Income tax expense	(319)	(868)	(460)	(2,024)
Net earnings	\$1,277	\$1,803	\$1,841	\$4,250
Basic earnings per share	\$0.09	\$0.13	\$0.13	\$0.30
Diluted earnings per share	\$0.09	\$0.13	\$0.13	\$0.30
Weighted average shares outstanding:				
Basic	13,997	13,969	13,988	14,103
Diluted	14,045	14,046	14,035	14,171

See accompanying notes to condensed consolidated financial statements.

Ballantyne Strong, Inc. and Subsidiaries

Condensed Consolidated Statements of Comprehensive Income

Three and Six Months Ended June 30, 2013 and 2012

(In thousands)

(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
Net earnings	\$1,277	\$1,803	\$1,841	\$4,250
Currency translation adjustment:				
Unrealized net change arising during period	(690)	(359)	(1,091)	(40)
Other Comprehensive Loss	(690)	(359)	(1,091)	(40)
Comprehensive Income	\$587	\$1,444	\$750	\$4,210

See accompanying notes to condensed consolidated financial statements.

Ballantyne Strong, Inc. and Subsidiaries**Condensed Consolidated Statements of Cash Flows****Six Months Ended June 30, 2013 and 2012****(In thousands)****(Unaudited)**

	Six Months Ended June 30, 2013 2012	
Net cash provided by (used in) operating activities	\$5,671	\$(5,724)
Cash flows from investing activities:		
Distribution from Joint Venture	—	1,509
Capital expenditures	(197)	(172)
Proceeds from sale of assets	2	3,043
Net cash (used in) provided by investing activities	(195)	4,380
Cash flows from financing activities:		
Excess tax benefits from share-based arrangements	(11)	—
Purchase of treasury stock	—	(2,667)
Proceeds from employee stock purchase plan	3	—
Net cash used in financing activities	(8)	(2,667)
Effect of exchange rate changes on cash and cash equivalents	(515)	(24)
Net increase (decrease) in cash and cash equivalents	4,953	(4,035)
Cash and cash equivalents at beginning of period	40,168	39,889
Cash and cash equivalents at end of period	\$45,121	\$35,854

See accompanying notes to condensed consolidated financial statements.

Ballantyne Strong, Inc. and Subsidiaries

Notes to the Condensed Consolidated Financial Statements

(Unaudited)

1. Nature of Operations

Ballantyne Strong, Inc. (“Ballantyne” or the “Company”), a Delaware corporation, and its wholly owned subsidiaries Strong Westrex, Inc., Strong Technical Services, Inc., Strong/MDI Screen Systems, Inc., and Strong Westrex (Beijing) Trading Inc., manufacture, distribute, integrate and service theatre and lighting systems on a worldwide basis.

The Company’s products are distributed to movie exhibition companies, sports arenas, auditoriums, amusement parks and special venues.

2. Summary of Significant Accounting Policies

Basis of Presentation and Principles of Consolidation

The condensed consolidated financial statements include the accounts of the Company and all majority owned and controlled domestic and foreign subsidiaries. All significant intercompany balances and transactions have been eliminated in consolidation.

The condensed consolidated financial statements included in this report are presented in accordance with the requirements of Form 10-Q and consequently do not include all of the disclosures normally required by accounting principles generally accepted in the United States of America for annual reporting purposes or those made in the Company’s Annual Report on Form 10-K. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year-ended December 31, 2012.

The condensed consolidated balance sheet as of December 31, 2012 was derived from the Company's audited consolidated balance sheet as of that date. All other condensed consolidated financial statements contained herein are unaudited and, in the opinion of management, reflect all adjustments of a normal recurring nature necessary to present a fair statement of the financial position and the results of operations and cash flows for the respective interim periods. The results for interim periods are not necessarily indicative of trends or results expected for a full year.

Use of Management Estimates

The preparation of condensed consolidated financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the condensed consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results and changes in facts and circumstances may alter such estimates and affect results of operations and financial position in future periods.

Fair Value of Financial and Derivative Instruments

The categorization within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. Financial assets and liabilities carried at fair value will be classified and disclosed in one of the following three categories:

- Level 1 - inputs to the valuation techniques are quoted prices in active markets for identical assets or liabilities
- Level 2 - inputs to the valuation techniques are other than quoted prices but are observable for the assets or liabilities, either directly or indirectly
- Level 3 - inputs to the valuation techniques are unobservable for the assets or liabilities

The following table presents the Company's financial assets and liabilities measured at fair value based upon the level within the fair value hierarchy in which the fair value measurements fall, as of June 30, 2013:

Fair Values Measured on a Recurring Basis:

	Level 1	Level 2	Level 3	Total
	\$ in thousands			
Cash and cash equivalents	\$45,121	\$—	\$—	\$45,121
Foreign currency forward contracts	\$—	\$8,021	\$—	\$8,021
Notes Receivable	\$—	\$—	\$2,232	\$2,232

The notes receivable accrue interest at a rate of 15% per annum which is paid in accordance with an agreed-upon cash flow schedule.

Quantitative information about the Company's level 3 fair value measurements at June 30, 2013 is set forth below:

\$ in thousands	Fair Value at 6/30/2013	Valuation Technique	Unobservable input	Range
Notes Receivable	\$ 2,232	Discounted cash flow	Probability of default	0 %
			Prepayment rates	0 %
			Loss severity	0 %

The significant unobservable inputs used in the fair value measurement of the Company's notes receivable are prepayment rates, probability of default and loss severity in the event of default. Significant increases (decreases) in any of these inputs in isolation would result in a significantly lower (higher) fair value measurement. Generally, a change in the assumption used for the probability of default is accompanied by a directionally similar change in the assumption used for the loss severity and directionally opposite change in the assumption used for prepayment rates.

The following table reconciles the beginning and ending balance of the Company's Notes Receivable fair value:

Six months ended June 30,	
2013	2012

	\$ in thousands	
Notes Receivable balance, beginning of period	\$2,232	\$2,062
Issuances of new notes	—	150
Notes Receivable balance, end of period	\$2,232	\$2,212

The following table presents the Company's financial assets and liabilities measured at fair value based upon the level within the fair value hierarchy in which the fair value measurements fall, as of December 31, 2012:

	Level 1	Level 2	Level 3	Total
	\$ in thousands			
Cash and cash equivalents	\$40,168	\$	—\$—	\$40,168
Notes Receivable	\$—	\$	—\$2,232	\$2,232

The carrying values of all other financial assets and liabilities including accounts receivable, accounts payable and accrued expenses reported in the consolidated balance sheets equal or approximate their fair values due to the short-term nature of these instruments. All non-financial assets that are not recognized or disclosed at fair value in the financial statements on a recurring basis, which includes non-financial long-lived assets, are measured at fair value in certain circumstances (for example, when there is evidence of impairment). During the six months ended June 30, 2013 we did not have any significant non-recurring measurements of non-financial assets or liabilities.

Recently Issued Accounting Pronouncements

There are no recently issued accounting pronouncements which the Company believes will materially impact its consolidated financial statements.

3. Earnings (Loss) Per Common Share

Basic earnings (loss) per share have been computed on the basis of the weighted average number of shares of common stock outstanding. Diluted earnings (loss) per share has been computed on the basis of the weighted average number of shares of common stock outstanding after giving effect to potential common shares from dilutive stock options and certain non-vested shares of restricted stock. The following table provides the reconciliation between basic and diluted earnings (loss) per share:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
(In thousands, except per share data)				
Basic earnings per share:				
Earnings (loss) applicable to common stock	\$1,277	\$1,803	\$1,841	\$4,250
Basic weighted average common shares outstanding	13,997	13,969	13,988	14,103
Basic earnings (loss) per share	\$0.09	\$0.13	\$0.13	\$0.30
Diluted earnings per share:				
Earnings (loss) applicable to common stock	\$1,277	\$1,803	\$1,841	\$4,250
Basic weighted average common shares outstanding	13,997	13,969	13,988	14,103
Dilutive effect of stock options and restricted stock awards	48	77	47	68
Dilutive weighted average common shares outstanding	14,045	14,046	14,035	14,171
Diluted earnings (loss) per share	\$0.09	\$0.13	\$0.13	\$0.30

For the three and six month periods ended June 30, 2013, grants and options to purchase 253,500 and 255,700 shares of common stock were outstanding but were not included in the computation of diluted earnings per share as the option's exercise price was greater than the average market price of the common shares for the respective periods. For the three and six month periods ended June 30, 2012, options to purchase 50,000 shares of common stock were outstanding but were not included in the computation of diluted earnings per share as the option's exercise price was greater than the average market price of the common shares for the respective periods.

4. Warranty Reserves

The Company has generally granted a warranty to its customers for a one-year period following the sale of manufactured and distributed products. In most instances, the distributed products are covered by the manufacturing firm's OEM warranty on parts and we cover warranty labor cost when required. However, there are certain customers where the Company may grant warranties in excess of the manufacturer's warranty for distributed products. The Company accrues for these costs at the time of sale or repair. The following table summarizes warranty activity for the three and six months ended June 30, 2013 and 2012:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2013	2012	2013	2012
(In thousands)				
Warranty accrual at beginning of period	\$760	\$1,051	\$770	\$1,028
Charged to expense	133	98	189	223
Amounts written off, net of recoveries	(48)	(297)	(116)	(406)
Foreign currency adjustment	6	(6)	8	1
Warranty accrual at end of period	\$851	\$846	\$851	\$846

5. Digital Link II Joint Venture

On March 6, 2007, the Company entered into an agreement with RealD to form an operating entity Digital Link II, LLC (the "LLC"). Under the agreement, the LLC was formed with the Company and RealD as the only two members with membership interests of 44.4% and 55.6%, respectively. The LLC was formed for purposes of commercializing certain 3D technology and to fund the deployment of digital projector systems and servers to exhibitors.

The Company accounts for its investment by the equity method. Under this method, the Company recorded its proportionate share of LLC net income or loss based on the LLC's financial statements as of June 21, 2013 and June 22, 2012, respectively. The LLC uses four 13-week periods for a total of 52 weeks to align its fiscal year-end with that of its majority interest holder, RealD. The Company's portion of loss of the LLC was \$0.01 million and \$0.1 million for the three and six months ended June 30, 2013. The Company's portion of income (loss) of the LLC was (\$0.02) million and \$0.1 million for the three and six months ended June 30, 2012, respectively.

In the past, the Company sold digital theatre projection equipment, in the normal course of business, to the LLC. The LLC in turn provides and sells the digital projection equipment to third party customers under system use agreements or through sales agreements. Revenue recognized by the Company on the sale transaction to the LLC is limited by its 44.4% ownership in the joint venture which will be recognized upon sale of the equipment to the third parties. There were no sales to the LLC during the three and six months ended June 30, 2013 and 2012. However, the Company recognized \$0 and \$0.2 million of gross margin during the three and six months ended June 30, 2012, respectively, related to the LLC's sale of equipment to third parties. The total receivable balance due from the LLC was insignificant at June 30, 2013 and December 31, 2012.

During the first quarter of 2012 the Company received a \$1.5 million return of investment in the LLC. The Company received no distributions from the LLC in the six months ended June 30, 2013.

6. Corporate-wide strategic initiative

In the fourth quarter of 2011, the Board of Directors and management of the Company approved a corporate-wide strategic initiative to refocus its worldwide digital equipment distribution business, services platform and cinema screen manufacturing business and exit the analog projector manufacturing business. The strategic initiative consisted of selling the Company's Omaha, Nebraska-based analog projector facility and manufacturing equipment and relocating its corporate headquarters to a new, smaller location in Omaha, which also houses its Network Operations Center. Total life to date severance charges for the strategic initiative begun in 2011 are approximately \$1.4 million. The strategic initiative is expected to be completed by the end of 2013.

The following table reconciles the beginning and ending restructuring balance for the six months ended June 30, 2013, which are included in accrued expenses:

	(in thousands)
Accrued severance at beginning of period	\$ 88
Severance paid	(27)
Accrued severance at end of period	\$ 61

7. Income Taxes

The effective tax rate (calculated as a ratio of income tax expense to pretax earnings, inclusive of equity method investment losses) was approximately 20.0% for the three and six months ended June 30, 2013, respectively as compared to 32.5% and 32.3% for the three and six months ended June 30, 2012, respectively. The effective tax rate differs from the statutory rates primarily as a result of differing foreign and U.S. tax rates applied to respective pre-tax earnings by tax jurisdiction. The Company's estimated annual effective rate was lower in the three and six months ended June 30, 2013 compared to the comparable periods of 2012 due to higher earnings before tax within our Canadian operations, Strong/MDI Screen Systems, Inc., which has a lower tax rate.

The Company's uncertain tax positions are related to tax years that remain subject to examination by the relevant taxable authorities. The Company has examinations not yet initiated for Federal purposes for fiscal years 2005 through 2012. In most cases, the Company has examinations open for State or local jurisdictions based on the particular jurisdiction's statute of limitations. The Company does not currently have any examinations in process. As of June 30, 2013, total unrecognized tax benefits amounted to approximately \$0.2 million.

8. Stock Compensation

The Company recognizes compensation expense for all share-based payment awards made to employees and directors based on their estimated fair values. Share-based compensation expense approximated the following for the three and six months ended June 30, 2013 and 2012 (in thousands):

	Three Months Ended June 30, 2013		Six Months Ended June 30, 2012	
Share based compensation expense	\$120	\$118)	\$220	\$279

Long-Term Incentive Plan

The Company's 2010 Long-Term Incentive Plan ("2010 Plan") provides the Compensation Committee of the Board of Directors with the discretion to grant stock options, stock appreciation rights, restricted shares, restricted stock units, performance shares, or performance units. Vesting terms vary with each grant and may be subject to vesting upon a "change in control" of the Company. The total number of shares reserved for issuance under the 2010 Plan was 600,000 shares. During the six months ended June 30, 2013, the Company awarded 22,500 options and 9,000 restricted stock shares under the 2010 Plan.

Options

As noted above, under the 2010 Plan, the Company granted options to purchase 22,500 shares of the Company's common stock during the six months ended June 30, 2013. Options to purchase shares of common stock were granted with exercise prices equal to the fair value of the common stock on the date of grant and vest over a four-year period. The fair value of stock options granted was estimated using a Black-Scholes valuation model with the following assumptions:

Expected dividend yield at date of grant	0	%
Expected stock price volatility	58.5	%
Risk-free interest rate	0.9	%
Expected life of options (in years)	5.5	

The risk-free interest rate assumptions were based on the U.S. Treasury yield curve in effect at the time of the grant. The expected volatility was based on historical monthly price changes of the Company's stock based on the expected

life of the options at the date of grant. The expected life of options is the average number of years the Company estimates that options will be outstanding. The Company considers groups of associates that have similar historical exercise behavior separately for valuation purposes.

The following table summarizes the Company's activities with respect to its stock options for the six months ended June 30, 2013 as follows:

	Number of Options	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding at December 31, 2012	191,200	\$ 5.64	8.69	\$ —
Granted	22,500	3.55		
Exercised	—	—		
Forfeited	—	—		
Outstanding at June 30, 2013	213,700	\$ 5.42	8.34	\$ 15,405
Exercisable at June 30, 2013	70,283	\$ 6.40	7.93	\$ 330

The aggregate intrinsic value in the table above represents the total that would have been received by the option holders if all in-the-money options had been exercised on June 30, 2013.

The following table summarizes information about stock options outstanding and exercisable at June 30, 2013:

Range of option exercise price	Options Outstanding at June 30, 2013			Options Exercisable at June 30, 2013		
	Number of options	Weighted average remaining contractual life	Weighted average exercise price per option	Number of options	Weighted average remaining contractual life	Weighted average exercise price per option
\$3.55 to 8.32	213,700	8.34	\$ 5.42	70,283	7.93	\$ 6.40

Restricted Stock Plans

The Company's 2005 Restricted Stock Plan (the "2005 Plan") provides for the grant of restricted stock awards. A total of 250,000 shares were reserved for issuance under the 2005 Plan. These shares are subject to such restrictions on transferability and other restrictions, if any, as the Compensation Committee may impose. During the six months ended June 30, 2013, the Company awarded 41,000 restricted shares under the 2005 Plan, which vest annually over a three year period.

The Ballantyne Strong, Inc. Non-Employee Directors' Restricted Stock Plan (the "Non-Employee Plan") provides for the award of restricted shares to outside directors. A total of 250,000 shares are reserved for issuance under the Non-Employee Plan. During the six months ended June 30, 2013, the Company granted 37,500 restricted shares under the Non-Employee Plan to the Board of Directors. These shares will vest the day preceding the Company's 2014 Annual Meeting of Stockholders.

In connection with the restricted stock granted to certain employees and non-employee directors, the Company accrues compensation expense based on the estimated number of shares expected to be issued utilizing the most current information available to the Company at the date of the financial statements. The Company estimates the fair value of restricted stock awards based upon the market price of the underlying common stock on the date of grant.

As of June 30, 2013, the total unrecognized compensation cost related to non-vested restricted stock awards was approximately \$0.8 million which is expected to be recognized over a weighted average period of 2.2 years.

The following table summarizes restricted stock activity for the six months ended June 30, 2013:

	Number of Restricted Stock Shares	Weighted Average Grant Price Fair Value
Non-vested at December 31, 2012	84,200	\$ 5.24
Granted	87,500	4.28
Shares vested	(42,200)	5.78
Shares forfeited	—	—
Non-vested at June 30, 2013	129,500	\$ 4.42

Employee Stock Purchase Plan

The estimated grant date fair value of purchase rights outstanding under the Employee Stock Purchase Plan at June 30, 2013 was \$1.51 per share using the Black-Scholes option-pricing model made with the following weighted average assumptions:

Expected dividend yield at date of grant	0	%
Expected stock price volatility	27.00	%
Risk-free interest rate	0.14	%
Expected term (in years)	1	

The Company recorded insignificant share-based compensation expense pertaining to the stock purchase plan with insignificant associated tax benefits for each of the three and six months ended June 30, 2013 and 2012. At June 30, 2013, the total unrecognized estimated compensation cost was insignificant.

9. Foreign Exchange Contracts

The Company's primary exposure to foreign currency fluctuations pertains to its subsidiaries in Canada and China. In certain instances the Company may enter into foreign exchange forward contracts to manage a portion of this risk. The Company has not designated its foreign exchange forward contracts as hedges.

The following table presents the gross fair value of derivative instrum