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MICROPAC INDUSTRIES INC  
Form 10QSB  
October 12, 2004

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

FORM 10 QSB

OMB Approval  
OMB Number XXXX-XXXX  
Expires Approval Pending  
Estimated Average Burden Hours Per Response 1.0

Quarterly Report Under Section 13 or 15 (d)  
of the Securities Exchange Act of 1934

for the Quarter Ended August 28, 2004

For the Transition Period from \_\_\_\_\_ to \_\_\_\_\_  
Commission File Number 0-5109

MICROPAC INDUSTRIES, INC.

|   |  |
|---|--|
| Delaware<br>-----<br>(State of Incorporation)                                     | 75-1225149<br>-----<br>(IRS Employer Identification No.) |
| 905 E. Walnut, Garland, Texas<br>-----<br>(Address of Principal Executive Office) | 75040<br>-----<br>(Zip Code)                             |
| Registrant's Telephone Number, including Area Code                                | (972) 272-3571<br>-----                                  |

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act of 1934 during the past 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  \_\_\_\_\_

At August 28, 2004 there were 3,078,315 shares issued and 2,578,315 shares of registrant's common stock outstanding. The aggregate market value of Common Stock could not be determined since there is no established public trading market for the Company's Common Stock.

MICROPAC INDUSTRIES, INC.

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FORM 10-QSB

AUGUST 28, 2004

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PART I - FINANCIAL INFORMATION

MICROPAC INDUSTRIES, INC.  
 CONDENSED STATEMENTS OF OPERATIONS  
 (Dollars in thousands except share data)  
 (Unaudited)

ITEM 1 - FINANCIAL STATEMENTS

|  | Three months ended |           | Year-to-date |           |
|--|--------------------|-----------|--------------|-----------|
|  | 08/28/04           | 08/30/03  | 08/28/04     | 08/30/03  |
|  | -----              | -----     | -----        | -----     |
| NET SALES  | \$ 4,242           | \$ 3,372  | \$ 11,411    | \$ 8,711  |
| COST AND EXPENSES:                                   |                    |           |              |           |
| Cost of goods sold                                   | (2,937)            | (2,338)   | (7,720)      | (6,811)   |
| Research and development                             | (127)              | (33)      | (231)        | (231)     |
| Selling, general & administrative expenses           | (685)              | (611)     | (1,971)      | (1,971)   |
|  | -----              | -----     | -----        | -----     |
| Total cost and expenses                              | 3,749              | 2,982     | 9,922        | 9,013     |
| OPERATING INCOME BEFORE INTEREST<br>AND INCOME TAXES | 493                | 390       | 1,489        | (302)     |
| Interest income                                      | 9                  | 22        | 19           | 19        |
|  | -----              | -----     | -----        | -----     |
| INCOME BEFORE TAXES                                  | \$ 502             | \$ 412    | \$ 1,508     | \$ (264)  |
| Provision for taxes                                  | (191)              | (156)     | (573)        | (573)     |
|  | -----              | -----     | -----        | -----     |
| NET INCOME   | \$ 311             | \$ 256    | \$ 935       | \$ (837)  |
|  | =====              | =====     | =====        | =====     |
| NET INCOME PER SHARE, BASIC AND DILUTED              | \$ 0.12            | \$ 0.08   | \$ 0.36      | \$ (0.27) |
| DIVIDENDS PER SHARE                                  | \$ --              | --        | \$ 0.05      | \$ --     |
| WEIGHTED AVERAGE OF SHARES, Basic and diluted        | 2,578,315          | 3,066,169 | 2,578,315    | 3,066,169 |

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These statements reflect all adjustments, which in the opinion of management are necessary for fair statement of the results for the interim period.

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MICROPAC INDUSTRIES, INC.  
CONDENSED BALANCE SHEETS  
(Dollars in thousands)  
(Unaudited)

ASSETS

| CURRENT ASSETS  | 8/28/04  | 11/30/03 |
|---|----------|----------|
|   | -----    | -----    |
| Cash and cash equivalents   | \$ 1,487 | \$ 2,337 |
| Short term investments  | 1,906    | 812      |
| Receivables, net of allowance for doubtful accounts of \$122 on August 28, 2004 and \$89 on November 30, 2003 | 2,197    | 1,877    |
| Inventories:  |          |          |
| Raw materials   | 1,241    | 692      |
| Work-in process   | 1,196    | 1,097    |
| Total Inventories   | 2,437    | 1,789    |
| Prepaid expenses and other current assets   | 85       | 71       |
| Deferred income tax   | 386      | 386      |
|   | -----    | -----    |
| Total current assets  | 8,498    | 7,272    |
|   | -----    | -----    |
| PROPERTY, PLANT AND EQUIPMENT, at cost:   |          |          |
| Land  | 80       | 80       |
| Buildings   | 498      | 498      |
| Facility improvements   | 797      | 797      |
| Machinery and equipment   | 5,151    | 5,027    |
| Furniture and fixtures  | 479      | 489      |
|   | -----    | -----    |
| Total property, plant, and equipment  | 7,005    | 6,891    |
| Less accumulated depreciation   | (6,035)  | (5,889)  |
|   | -----    | -----    |
| Net property, plant and equipment   | 970      | 1,002    |
|   | -----    | -----    |
| Total assets  | \$ 9,468 | \$ 8,274 |
|   | =====    | =====    |

LIABILITIES AND SHAREHOLDERS' EQUITY

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|  |          |          |
|--|----------|----------|
| CURRENT LIABILITIES:   |          |          |
| Accounts payable   | \$ 547   | \$ 308   |
| Accrued compensation   | 270      | 239      |
| Accrued professional fees  | 33       | 23       |
| Other accrued liabilities  | 412      | 249      |
| Income taxes payable   | 55       | 110      |
|  | -----    | -----    |
| Total current liabilities  | 1,317    | 929      |
|  | -----    | -----    |
| DEFERRED INCOME TAXES  | 69       | 69       |
| SHAREHOLDERS' EQUITY   |          |          |
| Common stock, (\$.10 par value), authorized 10,000,000 shares,<br>3,078,315 issued 2,578,315 outstanding at August 28, 2004 and<br>November 30, 2003 | 308      | 308      |
| Paid-in capital  | 885      | 885      |
| Treasury stock, 500,000 shares, at cost  | (1,250)  | (1,250)  |
| Retained earnings  | 8,139    | 7,333    |
|  | -----    | -----    |
| Total shareholders' equity   | 8,082    | 7,276    |
|  | -----    | -----    |
| Total liabilities and shareholders' equity   | \$ 9,468 | \$ 8,274 |
|  | =====    | =====    |

These statements reflect all adjustments, which in the opinion of management are necessary for fair statement of the results for the interim period.

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MICROPAC INDUSTRIES, INC.  
CONDENSED STATEMENTS OF CASH FLOWS  
(Dollars in thousands)  
(Unaudited)

|  | 8/28/04 | 8/30/03 |
|--|---------|---------|
|  | -----   | -----   |
| CASH FLOWS FROM OPERATING ACTIVITIES:      |         |         |
| Net Income                                 | \$ 935  | \$ 328  |
| Adjustments to reconcile net income to:    |         |         |
| Cash from operating activities:            |         |         |
| Depreciation and amortization              | 164     | 151     |
| Changes in current assets and liabilities: |         |         |
| Accounts receivable                        | (320)   | 124     |
| Inventories                                | (648)   | 222     |
| Prepaid expenses and other current assets  | (14)    | (17)    |
| Income taxes, prepaid and deferred         | (55)    | 5       |
| Accounts payable                           | 239     | (82)    |
| Payroll and withholdings                   | 31      | (48)    |
| Accrued liabilities                        | 173     | 24      |

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|   |            |          |
|---|------------|----------|
|   | -----      | -----    |
| Net cash provided by operating activities           | \$ 505     | \$ 707   |
| CASH FLOWS FROM INVESTING ACTIVITIES:               |            |          |
| Changes in investments                              | \$ (1,094) | \$ 1,124 |
| Additions to property, plant and equipment          | (115)      |          |
|   | -----      | -----    |
|   |            | (132)    |
| Net cash (used in) provided by investing activities | (1,226)    | 1,009    |
| CASH FLOWS FROM FINANCING ACTIVITIES                |            |          |
| Repurchase of common stock                          | --         | (1,471)  |
| Cash dividend                                       | (129)      | (312)    |
|   | -----      | -----    |
| Net cash used in financing activities               | (129)      | (1,783)  |
|   | -----      | -----    |
| Net change in cash and cash equivalents             | (850)      | (67)     |
| Cash and cash equivalents at beginning of period    | 2,337      | 1,296    |
|   | -----      | -----    |
| Cash and cash equivalents at end of period          | \$ 1,487   | \$ 1,229 |
|   | =====      | =====    |
| Supplemental cash flow disclosure                   |            |          |
| Cash paid for income taxes                          | \$ 633     | \$ 194   |
|   | =====      | =====    |

These statements reflect all adjustments, which, in the opinion of management, are necessary for fair statement of the results for the interim period.

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In the opinion of management, the unaudited consolidated financial statements include all adjustments (consisting of only normal, recurring adjustments) necessary to present fairly the financial position as of August 28, 2004, the results of operations for the three months and nine months ended August 28, 2004 and August 30, 2003, and the cash flows for nine months ended August 28, 2004 and August 30, 2003. Unaudited financial statements are prepared on a basis substantially consistent with those audited for the year ended November 30, 2003. The results of operations for the interim periods presented may not be indicative of total results for the full year. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles in the United States have been condensed or omitted pursuant to the rules and regulations promulgated by the Securities and Exchange Commission. However, management believes that the disclosures contained are adequate to make the information presented not misleading.

### Note 2

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

### Note 3

On January 28, 2003, the Board of Directors of Micropac Industries, Inc. approved the payment of a \$.10 per share dividend to all shareholders of record on February 10, 2003. The dividend payment was paid to shareholders on February 28, 2003.

On January 8, 2004, the Board of Directors of Micropac Industries, Inc. approved the payment of a special dividend of \$0.05 per share for shareholders of record as of January 30, 2004. This dividend was paid to the Company's shareholders on February 13, 2004.

### Note 4

On March 1, 2001, the Company's shareholders approved the 2001 Employee Stock Option Plan (the "Stock Plan"). As of August 28, 2004 there were 500,000 options available to be granted. No options have been granted to date.

### Note 5

During fiscal 2004, the Company renewed an uncollateralized \$3,000,000 line of credit agreement with a bank. The interest rate is equal to the prime rate less 1/4%. The line of credit requires that the Company maintain certain financial ratios and management personnel requirements. The Company has not borrowed against the line of credit to date.

### Note 6

Basic and diluted earnings per share are computed based upon the weighted average number of shares outstanding during the year. Diluted earnings per share gives effect to all dilutive potential common shares. For the nine months ended August 28, 2004 and August 30, 2003, the Company had no dilutive potential common stock.

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### Note 7

Effective May 1, 2004, the Company and Ms. Wood, Chief Executive Officer and President of the Company entered into a three (3) year employment agreement at a base salary of \$180,000 per annum.

Effective February 1, 2004, the Company and Mr. King, Chief Operating Officer and Vice President of the Company entered into a two (2) year employment agreement at a base salary of \$150,000 per annum.

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Effective February 1, 2004, the Company and Mr. Cefalu, Chief Financial Officer and Vice President of the Company entered into a two (2) year employment agreement at a base salary of \$82,000 per annum.

### Note 8

Glast, Phillips & Murray, P.C. serves as the Company's legal counsel. Mr. James K. Murphey, a director and member of the Company's audit committee, is a member of Glast, Phillips & Murray, P.C.

### Note 9

Effective May 13, 2002, the Company's Board of Directors approved the formation of an audit committee composed of the four (4) members of the Board. It is possible that three members of the audit committee, Messrs. Hempel, Wood and Murphey, may resign from the committee if future Securities and Exchange Commission rules establish a criteria that such individuals are not independent due to their relationships with the Company.

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## MICROPAC INDUSTRIES, INC. (Unaudited)

### ITEM 2 - MANAGEMENT DISCUSSION AND ANALYSIS OF THE FINANCIAL CONDITION AND RESULTS OF OPERATIONS

#### Results of Operations

|   | Three months ended |           | Year to Date |           |
|---|--------------------|-----------|--------------|-----------|
|   | 8/28/2004          | 8/30/2003 | 8/28/2004    | 8/30/2003 |
| NET SALES   | 100.00%            | 100.00%   | 100.00%      | 100.00%   |
| COST AND EXPENSES                                 |                    |           |              |           |
| Cost of goods sold                                | 69.24%             | 69.33%    | 67.66%       | 70.63%    |
| Research and development                          | 2.99%              | 0.98%     | 2.02%        | 2.44%     |
| Selling, general & administrative                 | 16.15%             | 18.12%    | 17.27%       | 21.81%    |
|   | -----              | -----     | -----        | -----     |
| Total cost and expenses                           | 88.38%             | 88.43%    | 86.95%       | 94.88%    |
| OPERATING INCOME BEFORE INTEREST AND INCOME TAXES | 11.62%             | 11.57%    | 13.05%       | 5.12%     |
| Interest income                                   | 0.21%              | 0.65%     | 0.17%        | 0.59%     |
|   | -----              | -----     | -----        | -----     |
| INCOME BEFORE TAXES                               | 11.83%             | 12.22%    | 13.22%       | 5.71%     |
| Provision for taxes                               | 4.50%              | 4.63%     | 5.02%        | 2.16%     |
|   | -----              | -----     | -----        | -----     |
| NET INCOME  | 7.33%              | 7.59%     | 8.20%        | 3.55%     |

Sales for the third quarter and first nine months ended August 28, 2004 totaled \$4,242,000 and \$11,411,000, respectively. Sales for the third quarter increased 25.8% or \$870,000 above sales for the same period of 2003, while sales for the first nine months of 2004 increased 23.5% or \$2,169,000 above the first nine months of 2003. The increase in sales is primarily attributable to improved business conditions in the company's major market segments, combined with the introduction of new products. Sales for the first nine months of 2004 compared to 2003 increased 24% in the commercial market, 19% in the military market, and 38% in the space market.

Cost of goods sold for the third quarter 2004 versus 2003 totaled 69.3% and 69.3% of net sales, respectively, while cost of goods sold for the nine months of the comparable period totaled 67.7% and 70.6%, respectively. The cost of goods sold decrease of 2.9% is attributable to higher sales volume, changes in product mix, and yield improvements on certain products.

Selling, general and administrative expenses for the third quarter and first

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nine months of 2004 totaled 16.2% and 17.2%, respectively, compared to 18.1% and 21.8% for the same period in 2003. In actual dollars expensed, selling, general and administrative expenses increased \$74,000 in the third quarter of 2004, compared to 2003, and decreased \$45,000 for the first nine months of 2004, versus 2003, attributable to lower general and administrative salaries.

Net income in the third quarter and year to date 2004 totaled \$311,000 and \$935,000, respectively, compared to \$256,000 and \$328,000 for the comparable periods in 2003. Net income per share totaled \$.36 and \$.11 for the comparable nine months of 2004 and 2003, respectively. The increase in net income is associated with higher sales, lower cost as a % of sales, and continued control of overhead and general and administrative expenses.

New orders for the third quarter and year-to-date 2004 totaled \$5,158,000 and \$15,456,000, respectively, compared to \$2,752,000 and \$8,346,000 for the comparable periods of 2003.

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Backlog totaled \$7,809,000 on August 28, 2004 compared to \$4,203,000 as of August 30, 2003 and \$5,594,000 on November 30, 2003.

Total assets increased \$1,194,000 to \$9,468,000 as of August 28, 2004 from \$8,274,000 as of November 30, 2003 with an increase in cash and short-term investments of \$244,000, inventory increase of \$648,000, accounts receivable increase of \$320,000, increase in prepaid expense of \$14,000, and a decrease in net property, plant, and equipment of \$32,000.

Accounts receivable, net totaled \$2,197,000 as of August 28, 2004 and represents an increase of \$320,000 since November 30, 2003, due to increased sales.

Inventories totaled \$2,437,000 at the end of the third quarter 2004 compared to \$1,789,000 on November 30, 2003, an increase of \$648,000. Raw materials inventories increased \$549,000 since November 30, 2003, while work-in-process inventories increased \$99,000. The increase in raw materials is attributable to the purchase and receipt of long lead-time material which was funded by the customer, and an increase of piece parts to support the higher sales volume.

Current liabilities totaled \$1,316,000 on August 28, 2004 representing an increase of \$387,000 from November 30, 2003; primarily associated with an increase in accounts payable of \$239,000 due to increased materials purchases to support the higher sales volume, an increase of \$31,000 in accrued payroll, a reduction of \$55,000 in provision for income taxes, an increase in other accrued liabilities of \$163,000 based on higher reserves associated with advance payments from customers, and an increase of \$10,000 accrued professional fees.

Shareholders' equity increased \$807,000 in the first nine months of 2004. Earnings per share for the nine month period totaled \$.36 per share.

### Liquidity and Capital Resources

-----

Cash and short-term investments as of August 28, 2004 totaled \$3,393,000 compared to \$3,149,000 on November 30, 2003, an increase of \$244,000.

As of August 28, 2004 cash flows from operating activities were \$505,000 compared to \$707,000 as of August 30, 2003.

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Capital expenditures through the third quarter of 2004 totaled \$132,000 compared to \$115,000 as of August 30, 2003. These purchases were financed internally with the Company's cash.

A special cash dividend of \$129,000 was paid on February 13, 2004 to all shareholders of record.

During fiscal 2004, the Company renewed an uncollateralized \$3,000,000 line of credit agreement with a bank. The interest rate is equal to the prime rate less 1/4%. The line of credit requires that the Company maintain certain financial ratios and management personnel requirements. The Company has not borrowed against the line of credit to date.

The Company expects to generate adequate amounts of cash from the sale of products and services and the collection thereof to meet its liquidity needs.

### Outlook

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New orders for the third quarter and year-to-date 2004 totaled \$5,158,000 and \$15,456,000, respectively, compared to \$2,752,000 and \$8,346,000 for the comparable periods of 2003. The Company's major new orders received in the third quarter of 2004 were for custom design assemblies and microcircuits for industrial applications, custom and new products for military and space applications and standard optoelectronics products sold through distribution channels. Orders in the fourth quarter are not expected to keep pace with orders in the prior three (3) quarters.

Backlog totaled \$7,809,000 on August 28, 2004 compared to \$4,203,000 as of August 30, 2003 and \$5,594,000 on November 30, 2003. The majority of the backlog is shippable in the next twelve (12) months and represents a good mix of the company's products and technologies with 17% in the commercial market, 54% in the military market, and 29% in the space market.

### Cautionary Statement

This Form 10-QSB contains forward-looking statements that are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Actual results could differ materially. Investors are warned that forward-looking statements involve risks and unknown factors including, but not limited to, customer cancellation or rescheduling of orders, problems affecting delivery of vendor-supplied raw materials and components, unanticipated manufacturing problems and availability of direct labor resources. The Company disclaims any responsibility to update the forward-looking statements contained herein, except as may be required by law.

### ITEM 3. CONTROLS AND PROCEDURES

#### (a) Evaluation of disclosure controls and procedures.

As of August 28, 2004, the Company carried out an evaluation, under the supervision and with participation of the Company's management, including the Chief Executive Officer and Chief Financial Officer, of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Exchange Act Rule 13a-14. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer

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concluded that the Company's disclosure controls and procedures are effective in timely alerting them to material information relating to the Company required to be included in the Company's quarterly SEC filings.

(b) Changes in internal controls.

Not applicable.

### PART II - OTHER INFORMATION

#### ITEM 1. LEGAL PROCEEDINGS

The Company is not involved in any material current or pending legal proceedings.

#### ITEM 2. CHANGES IN SECURITIES

None

#### ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None

#### ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None

#### ITEM 5. OTHER INFORMATION

None

#### ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

31.1 Certification of Connie Wood, President and CEO (Principal Executive Officer) Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

31.2 Certification of Patrick Cefalu, CFO (Principal Financial Officer) Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002

32.1 Certification of Connie Wood, President and CEO (Principal Executive Officer), Pursuant to 18 U.S.C. Section 906 of the Sarbanes-Oxley Act of 2002

32.2 Certification of Patrick Cefalu, CFO (Principal Financial Officer), Pursuant to 18 U.S.C. Section 906 of the Sarbanes-Oxley Act of 2002.

(b) Reports on Form 8-K

At a Board of Directors meeting held on May 11, 2004, the Board of Directors unanimously elected Mr. Nicholas Nadolsky as a Member and Chairman of the Board, to serve in such positions until the next annual meeting of shareholders or until his earlier death, resignation or removal from office. There is no employment agreement between Mr. Nadolsky and the Company. Since 1980, the Company has leased a 4800 square foot building from Mr. Nadolsky, at a current annual rental of

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\$39,600.

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SIGNATURES

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

MICROPAC INDUSTRIES, INC.

October 11 , 2004  
-----

Date

/s/ Connie Wood  
-----

Connie Wood  
Chief Executive Officer

October 11 , 2004  
-----

Date

/s/ Patrick Cefalu  
-----

Patrick Cefalu  
Chief Financial Officer

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