

PEAK INTERNATIONAL LTD
Form 10-Q
February 13, 2003

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended December 31, 2002

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 0-29332

PEAK INTERNATIONAL LIMITED

(Exact Name of Registrant as Specified in its Charter)

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Incorporated in Bermuda with limited liability
(State or other jurisdiction of incorporation or organization)

None
(I.R.S. Employer Identification Number)

44091 Nobel Drive, P.O. Box 1767, Fremont, California
(Address of principal executive offices)

94538
(Zip Code)

(510) 449-0100

(Registrant's telephone number)

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 is an accelerated filer (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 February 10, 2003.

Class
Common Stock, \$0.01 Par Value

Outstanding at February 10, 2003
12,700,912

PART I

FINANCIAL INFORMATION

Item 1. *Financial Statements*

Condensed Consolidated Statements of Operations and Comprehensive Income (Loss)

(in thousands of United States Dollars, except share and per share data)

	Three Months Ended December 31,			
	2002		2001	
	(Unaudited)		(Unaudited)	
Net Sales:				
Third parties	\$ 15,115		\$ 12,189	
Related companies				
	15,115	100.0%	12,189	100.0%
Cost of Goods Sold	10,176	67.3%	8,380	68.8%
Gross Profit	4,939	32.7%	3,809	31.2%
General and Administrative	1,687	11.2%	2,000	16.4%
Research and Development	36	0.2%	24	0.2%
Selling and Marketing (Note 3)	2,697	17.8%	2,007	16.4%
Asset impairment (Note 13)	100	0.7%		0.0%
Operating Income (Loss)	419	2.8%	(222)	(1.8)%
Other Income (Expenses) net	53	0.3%	(50)	(0.4)%
Interest Income	76	0.5%	127	1.0%
Income (Loss) Before Tax	548	3.6%	(145)	(1.2)%
Income Tax Expense	206	1.3%	85	0.7%
Net Income (Loss)	\$ 342	2.3%	\$ (230)	(1.9)%
Other comprehensive income (loss):				
Foreign currency translation adjustment	(42)		37	
Comprehensive income (loss)	\$ 300		\$ (193)	
EARNINGS (LOSS) PER SHARE				
Basic	\$ 0.03		\$ (0.02)	
Diluted	\$ 0.03		\$ (0.02)	

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Weighted Average Number of Shares (in thousands)		
Basic	12,699	12,740
	<u> </u>	<u> </u>
Diluted	12,742	12,740
	<u> </u>	<u> </u>

	Nine Months Ended December 31,			
	2002		2001	
	(Unaudited)		(Unaudited)	
Net Sales:				
Third parties	\$ 41,915		\$ 32,561	
Related companies			1,120	
	<u>41,915</u>	100.0%	<u>33,681</u>	100.0%
Cost of Goods Sold (Note 2)	<u>31,301</u>	74.7%	<u>27,397</u>	81.3%
Gross Profit	10,614	25.3%	6,284	18.7%
General and Administrative	5,941	14.2%	6,885	20.5%
Research and Development	103	0.2%	119	0.4%
Selling and Marketing (Note 3)	7,447	17.8%	6,002	17.8%
Asset Impairment (Note 13)	10,584	25.2%		0.0%
Operating Loss	<u>(13,461)</u>	(32.1)%	<u>(6,722)</u>	(20.0)%
Other Expenses net	(40)	(0.1)%	(148)	(0.4)%
Interest Income	231	0.5%	631	1.9%
Loss Before Tax	<u>(13,270)</u>	(31.7)%	<u>(6,239)</u>	(18.5)%
Income Tax Expense (Benefit)	157	0.3%	(5)	0.0%
Net Loss	\$ <u>(13,427)</u>	(32.0)%	\$ <u>(6,234)</u>	(18.5)%
Other comprehensive loss:				
Foreign currency translation adjustment	(79)		134	
Comprehensive loss	\$ <u>(13,506)</u>		\$ <u>(6,100)</u>	
LOSS PER SHARE				
Basic	\$ <u>(1.06)</u>		\$ <u>(0.48)</u>	
Diluted	\$ <u>(1.06)</u>		\$ <u>(0.48)</u>	
Weighted Average Number of Shares (in thousands)				
Basic	<u>12,689</u>		<u>12,997</u>	
Diluted	<u>12,689</u>		<u>12,997</u>	

(See accompanying notes to Condensed Consolidated Financial Statements)

Condensed Consolidated Balance Sheets

(in thousands of United States Dollars, except share and per share data)

	December 31, 2002	March 31, 2002
	(Unaudited)	
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 26,708	\$ 29,217
Accounts receivable net of allowance for doubtful accounts of \$288 at December 31, 2002 and \$241 at March 31, 2002	10,790	8,200
Inventories (Note 4)	11,795	12,325
Other receivables, deposits and prepayments	1,068	1,396
Income taxes receivable		156
	<u>50,361</u>	<u>51,294</u>
Total Current Assets		
Asset to be disposed of by sale (Note 13)	8,024	
	<u>8,024</u>	
Long Term Assets:		
Deposits for Acquisition of Property, Plant and Equipment	47	67
Land Use Rights	786	1,967
Property, Plant and Equipment net	28,991	50,488
Income taxes receivable (Note 5)	3,070	
Other deposit (Note 6)	300	
	<u>33,194</u>	<u>52,522</u>
Total Long Term Assets		
TOTAL	\$ 91,579	\$ 103,816
LIABILITIES AND STOCKHOLDERS EQUITY		
Current Liabilities:		
Accounts payable:		
Trade	\$ 3,630	\$ 2,493
Property, plant and equipment		705
Accrued payroll and employee benefits	1,631	1,021
Accrued other expenses	1,549	1,614
Income taxes payable	5,678	5,424
	<u>12,488</u>	<u>11,257</u>
Total Current Liabilities		
Deferred Income Taxes	1,664	1,777
	<u>14,152</u>	<u>13,034</u>
Total Liabilities		
Commitments and Contingencies (Note 11)		
Stockholders Equity:		
Common stock, \$0.01 par value; authorized 100,000,000 shares; issued and outstanding 12,692,803 shares at December 31, 2002, and 12,664,324 shares at March 31, 2002	127	127
Additional paid-in capital	28,119	27,968

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Retained earnings	50,357	63,784
Accumulated other comprehensive loss	(1,176)	(1,097)
	<u>77,427</u>	<u>90,782</u>
Total stockholders' equity	77,427	90,782
	<u>77,427</u>	<u>90,782</u>
TOTAL	\$ 91,579	\$ 103,816
	<u>\$ 91,579</u>	<u>\$ 103,816</u>

(See accompanying notes to Condensed Consolidated Financial Statements)

Condensed Consolidated Statements of Cash Flows

(in thousands of United States Dollars)

	Nine Months Ended	
	December 31,	
	2002	2001
	(Unaudited)	(Unaudited)
Operating activities:		
Net loss	\$ (13,427)	\$ (6,234)
Adjustments to reconcile net loss to net cash (used in) provided by operating activities:		
Depreciation and amortization	4,731	4,599
Deferred income taxes	(113)	171
Loss on write-off/disposal of property, plant and equipment	534	73
Allowance for doubtful accounts	54	(16)
Asset impairment	10,584	
Changes in operating assets and liabilities:		
Accounts receivable, net	(2,644)	1,386
Inventories	530	2,064
Other receivables, deposits and prepayments	328	(8)
Income taxes receivable	(2,914)	(7)
Other deposit	(300)	
Accounts payable trade	1,137	(538)
Accrued payroll, employee benefits and other expenses	545	167
Amounts due from related companies		589
Income taxes payable	254	(293)
Net cash (used in) provided by operating activities	(701)	1,953
Investing activities:		
Proceeds on sales of property, plant and equipment	4	
Acquisition of property, plant and equipment	(1,900)	(1,614)
Decrease in deposits for acquisition of property, plant and equipment	20	86
Net cash used in investing activities	(1,876)	(1,528)
Financing activities:		
Payment for TrENDS		(3,080)
Payment for share buyback	(38)	(3,526)
Proceeds from issue of common stock	189	291
Net cash provided by (used in) financing activities	151	(6,315)
Net decrease in cash and cash equivalents	(2,426)	(5,890)
Effects of exchange rate changes on cash and cash equivalents	(83)	134
Cash and cash equivalents at beginning of period	29,217	33,901
Cash and cash equivalents at end of period	\$ 26,708	\$ 28,145
Supplemental cash flow information:		

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Cash paid during the period

Interest	\$	\$
Income taxes	2,930	136
	<u> </u>	<u> </u>

(See accompanying notes to Condensed Consolidated Financial Statements)

Notes to Condensed Consolidated Financial Statements

(in thousands of United States Dollars, except share and per share data, unaudited)

(1) Organization and basis of presentation

Peak International Limited (the Company) was incorporated as an exempted company with limited liability in Bermuda under the Companies Act 1981 of Bermuda (as amended) on January 3, 1997. The subsidiaries of the Company are principally engaged in the manufacture and sale of precision engineered packaging products, such as matrix and disk drive trays, shipping tubes, reels and carrier tapes, lead frame boxes and interleaves used in the storage and transportation of semiconductor devices and other electronic components. The Company's principal production facilities are located in the People's Republic of China (the PRC) and the Company maintains offices in Hong Kong, the United States of America, Singapore, Malaysia, the PRC, Taiwan, Italy and the Philippines.

The condensed consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intra-group balances and transactions have been eliminated on consolidation.

The accompanying condensed consolidated financial information has been prepared by the Company without audit, in accordance with the instructions to Form 10-Q and therefore does not include all information and footnotes necessary for a fair presentation of financial position, results of operations and cash flows in accordance with accounting principles generally accepted in the United States of America.

The preparation of financial statements in conformity with generally accepted accounting principles requires the use of estimates and assumptions that affect reported amounts of certain assets, liabilities, revenues and expenses as of and for the reporting periods. Actual results could differ from those estimates. Differences from those estimates are reported in the period they become known.

The unaudited condensed consolidated financial statements reflect all adjustments (including normal recurring adjustments) which in the opinion of management are required for a fair presentation of the Company's interim results. The results for interim periods are not necessarily indicative of the results that may be achieved in the entire year. These condensed consolidated financial statements and notes thereto should be read together with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended March 31, 2002.

(2) Cost of goods sold

Included therein was \$432 (unaudited) write-off of machinery and molds due to technological obsolescence and capacity under-utilization for the nine months ended December 31, 2002.

(3) Delivery and freight expenses

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For the quarter and for the nine months ended December 31, 2002, the Company incurred delivery and freight expenses of approximately \$765 (unaudited) and \$2,062 (unaudited) (2001 \$557 and \$1,397, unaudited) respectively, which have been included as part of selling and marketing expenses.

Notes to Condensed Consolidated Financial Statements (continued)

(in thousands of United States Dollars, except share and per share data, unaudited)

(4) Inventories

	December 31,	March 31,
	2002	2002
	<u>(Unaudited)</u>	<u>(Unaudited)</u>
Raw materials	\$ 6,452	\$ 7,463
Finished goods	5,343	4,862
	<u>\$ 11,795</u>	<u>\$ 12,325</u>

(5) Income Taxes Receivable

This represents approximately \$3,070 of tax reserve certificates purchased from the Inland Revenue Department (IRD) of Hong Kong in respect of prior year taxes that are under examination by the IRD. The placement of such certificates is a condition stipulated by the IRD.

There has been no change in the tax filing status of our Hong Kong subsidiaries since March 31, 2002.

(6) Other Deposit

This represents the security bond placed at a Taiwanese court in order to obtain an anti-injunction order in respect of a potential patent dispute in Taiwan. See Note 11(c) Other legal proceedings .

(7) Stock Options

Option activity relating to the Company's stock option plan is summarized as follows (unaudited):

Outstanding Options

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	Number of Shares	Weighted average exercise price per share
Outstanding at April 1, 2002	2,686,894	\$ 7.29
Granted	110,000	8.03
Exercised	(2,000)	3.66
Forfeited	(132,511)	9.01
	<hr/>	
Outstanding at June 30, 2002	2,662,383	7.24
Granted	103,500	4.81
Forfeited	(16,882)	10.34
	<hr/>	
Outstanding at September 30, 2002	2,749,001	7.13
Granted	363,500	3.58
Forfeited	(20,313)	9.52
	<hr/>	
Outstanding at December 31, 2002	3,092,188	6.70
	<hr/>	

Notes to Condensed Consolidated Financial Statements (continued)

(in thousands of United States Dollars, except share and per share data, unaudited)

	Outstanding Options	
	Number of	Weighted
		Shares
Outstanding at April 1, 2001	2,498,593	\$ 7.67
Exercised	(2,083)	5.38
Forfeited	(73,149)	8.09
Outstanding at June 30, 2001	2,423,361	7.66
Granted	380,868	6.21
Exercised	(2,906)	4.15
Forfeited	(38,610)	7.95
Outstanding at September 30, 2001	2,762,713	7.46
Granted	49,000	5.79
Forfeited	(85,814)	10.16
Outstanding at December 31, 2001	2,725,899	7.34
Exercised	(2,600)	4.98
Forfeited	(36,405)	10.97
Outstanding at April 1, 2002	2,686,894	7.29

(8) Earnings (Loss) Per Share

The following is a reconciliation of the numerator and the denominator of the basic and diluted earnings (loss) per share:

	Three Months Ended December 31,	
	2002	2001
Net Income (Loss) available to common shareholders (numerator)	(Unaudited) \$ 342	(Unaudited) \$ (230)
Shares Weighted average shares outstanding (denominator, in thousands)		
Basic	12,699	12,740
Assumed conversion of stock options	43	

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	12,742	12,740
Diluted		
Nine Months Ended		
December 31,		
	2002	2001
	(Unaudited)	(Unaudited)
Net Loss available to common shareholders (numerator)	\$ (13,427)	\$ (6,234)
Shares Weighted average shares outstanding (denominator, in thousands)		
Basic	12,689	12,997
Assumed conversion of stock options		
Diluted	12,689	12,997

Notes to Condensed Consolidated Financial Statements (continued)

(in thousands of United States Dollars, except share and per share data, unaudited)

For the quarter ended December 31, 2001, nine months ended December 31, 2002 and 2001, all stock options were anti-dilutive and therefore not included in the computation of diluted loss per share.

(9) Employee Stock Purchase and Option Plans

During the quarter ended December 31, 2002, the Company issued 50,000 options to an officer under the 1998 Stock Option Plan at an exercise price of \$4.00 per share and 313,500 options to officers under the 1998 Stock Option Plan at an exercise price of \$3.515 per share. The Company issued 13,241 shares to employees under contributions made during the quarter ended September 30, 2002, and authorized the issuance of 9,248 shares to employees under contributions made during the quarter ended December 31, 2002, under the 1998 Employee Stock Purchase Plan.

During the nine months ended December 31, 2002, the Company issued 110,000 options to employees under the 1997 Stock Option Plan at an exercise price of \$8.025 per share, 103,500 shares to outside directors and employees under the 1998 Stock Option Plan at an exercise price of \$4.81 per share, 50,000 options to an officer under the 1998 Stock Option Plan at an exercise price of \$4.00 per share and 313,500 options to officers under the 1998 Stock Option Plan at an exercise price of \$3.515 per share. The Company issued 36,706 shares to employees under contributions made during the nine months ended September 30, 2002.

(10) Share Repurchase

In September 2000, the Board of Directors of the Company authorized the repurchase by the Company of up to \$10,000 of its common stock at prices not to exceed 150% of the Company's net asset value per share. Common stock repurchased will be cancelled immediately. The excess of purchase price over par value is charged to additional paid-in capital.

In addition, pursuant to the authority granted by the Board of Directors, the Company purchased 473,876 units of Trust Enhanced Dividend Securities of Peak TrENDS Trust (TrENDS) at an average price of \$6.50 per TrENDS totaling \$3,080 through a tender offer. In May 2001, the shares obtained as a result of the automatic conversion of TrENDS into common shares were cancelled.

The Company repurchased 10,200 shares at an average price of \$3.76 during the quarter and nine months ended December 31, 2002.

(11) Commitments and Contingencies

(a) Litigation

On June 29, 1999, Dorchester Investors commenced a purported securities class action suit in the United States District Court for the Southern District of New York on behalf of all TrENDS purchasers against the Company, the Peak TrENDS Trust (the Trust), Mr. T.L. Li, Mr. Jerry Mo, Luckygold 18A Limited (Luckygold) and Donaldson, Lufkin & Jenrette Securities Corporation (DLJ). On June 5, 2000, the court dismissed the Company and Mr. Mo from the class action.

However, the Company has indemnity obligations to DLJ and the Trust (the primary indemnity) against losses incurred in connection with the TrENDS offering. The exposure of this indemnity may ultimately have a material impact to the financial statements of the Company. Mr. T.L. Li and Luckygold have provided a separate indemnity to the Company from liabilities (the counter indemnity) related to the TrENDS offering, including the exposure in relation to the indemnity obligations provided to DLJ and the Trust. The counter indemnity may partially, or even fully, cover the primary indemnity provided by the Company to certain defendants.

Notes to Condensed Consolidated Financial Statements (continued)

(in thousands of United States Dollars, except share and per share data, unaudited)

As of this date, the outcome of the class action and hence the effect of the primary and counter indemnity, is still contingent. The Company considers that it is not possible to reasonably estimate with any certainty the potential damages, if any, arising from this litigation. The Company has therefore not made any provision in the financial statements in this respect.

The Company was involved in an arbitration with Mr. Richard Brook, a former Chief Executive Officer. The result of the arbitration was a judgment in the amount of approximately \$520 in favor of the Company against Mr. Brook. The Company is uncertain whether it will be able to collect any portion of the judgment against Mr. Brook.

The Company, one of its officers, and a former employee are parties to a lawsuit filed on February 28, 2002 by a former employee in the Superior Court of California seeking unspecified damages for alleged race harassment, sex (pregnancy) discrimination, retaliation and wrongful termination. While the case is in its preliminary stages and its outcome cannot be predicted, the Company believes it has meritorious defenses to the allegations.

(b) Commitments

During the nine months ended December 31, 2002, the Company has settled a foreign exchange contract of \$1,000 primarily to sell Singapore dollars and it has no material impact on the Company's operating results.

At December 31, 2002, the Company had commitments for capital expenditures of approximately \$162.

(c) Other legal proceedings

R.H. Murphy Co., Inc. (Murphy) is the owner of U.S. Reexamined Patent 5,400,904 C1 and certain corresponding foreign patents, which patents are directed to specific features in trays used to carry integrated circuits. Murphy has notified the Company and certain of its customers that it believes these patents are infringed by certain integrated circuit trays that the Company provided to its customers, and indicated that licenses to these patents are available. The Company does not believe that any valid claim of these patents is infringed, and is proceeding consistent with that belief.

During the second quarter of fiscal 2003, a security bond of approximately \$300 was placed at a Taiwanese district court in order to obtain an anti-injunction order so that the Company can continue to sell trays in Taiwan without being interrupted by Murphy and its three distributors in Taiwan. The Taiwanese district court granted the order whereas Murphy's three local distributors filed an appeal with the Taiwanese high court against the grant of the order by the district court. The high court ruled that the anti-injunction order should be revoked and the Company has filed an appeal. In addition, the Company also filed an action with the Taiwanese Intellectual Property Office to invalidate Murphy's patent. The

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Company also filed a complaint for unfair competition with the Fair Trade Commission against Murphy. At present, the outcome of this potential patent dispute cannot be predicted with reasonable particularity and no impact to the financial statements has been reflected in this respect.

Notes to Condensed Consolidated Financial Statements (continued)

(in thousands of United States Dollars, except share and per share data, unaudited)

(12) Segment Information

	<u>Hong Kong & the PRC</u>	<u>United States</u>	<u>Other Asian countries</u>	<u>Eliminations</u>	<u>Consolidated</u>
Quarter ended December 31, 2002 (unaudited)					
Net sales to third parties	\$ 8,798	\$ 1,921	\$ 4,396	\$	\$ 15,115
Transfer between geographic areas	7,927		461	(8,388)	
Total net sales	<u>\$ 16,725</u>	<u>\$ 1,921</u>	<u>\$ 4,857</u>	<u>\$ (8,388)</u>	<u>\$ 15,115</u>
Income (Loss) before tax	<u>\$ 532</u>	<u>\$ 95</u>	<u>\$ 130</u>	<u>\$ (209)</u>	<u>\$ 548</u>
Quarter ended December 31, 2001 (unaudited)					
Net sales to third parties	\$ 6,791	\$ 990	\$ 4,408	\$	\$ 12,189
Transfer between geographic areas	4,926	196	581	(5,703)	
Total net sales	<u>\$ 11,717</u>	<u>\$ 1,186</u>	<u>\$ 4,989</u>	<u>\$ (5,703)</u>	<u>\$ 12,189</u>
Income (Loss) before tax	<u>\$ 439</u>	<u>\$ (424)</u>	<u>\$ (38)</u>	<u>\$ (122)</u>	<u>\$ (145)</u>
Nine months ended December 31, 2002 (unaudited)					
Net sales to third parties	\$ 26,109	\$ 5,054	\$ 10,752	\$	\$ 41,915
Transfer between geographic areas	19,568		1,323	(20,891)	
Total net sales	<u>\$ 45,677</u>	<u>\$ 5,054</u>	<u>\$ 12,075</u>	<u>\$ (20,891)</u>	<u>\$ 41,915</u>
(Loss) Income before tax	<u>\$ (12,975)</u>	<u>\$ 189</u>	<u>\$ (199)</u>	<u>\$ (285)</u>	<u>\$ (13,270)</u>
Nine months ended December 31, 2001 (unaudited)					
Net sales to third parties	\$ 18,955	\$ 2,965	\$ 10,641	\$	\$ 32,561
Net sales to related companies	1,120				1,120
Transfer between geographic areas	12,472	203	1,429	(14,104)	
Total net sales	<u>\$ 32,547</u>	<u>\$ 3,168</u>	<u>\$ 12,070</u>	<u>\$ (14,104)</u>	<u>\$ 33,681</u>
(Loss) Income before tax	<u>\$ (3,115)</u>	<u>\$ (2,470)</u>	<u>\$ (948)</u>	<u>\$ 294</u>	<u>\$ (6,239)</u>

(13) Asset to be disposed of by sale/asset impairment charge

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A subsidiary of the Company, operating in Shenzhen in the PRC, owns a factory under construction in the PRC. In view of its production needs and the market conditions, the completion of the factory under construction has been delayed. Management has continuously reviewed the asset for impairment given the downturn in the industrial property market.

The factory under construction and the related la