

XYRATEX LTD
Form 6-K
October 15, 2008

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 6-K

REPORT OF FOREIGN PRIVATE ISSUER PURSUANT TO RULE 13a-16 OR 15d-16 UNDER
THE SECURITIES EXCHANGE ACT OF 1934

October 15, 2008

Commission File Number:0001284823

XYRATEX LTD

(Translation of registrant's name into English)

Langstone Road,
Havant
PO9 1SA
United Kingdom

(Address of principal executive offices)

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or 40-F.

Form 20-F ☒ Form 40-F ☐

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(1) ☐

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(7) ☐

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Indicate by check mark whether the registrant by furnishing the information contained in this Form is also thereby furnishing the information to the Commission pursuant to rule 12g3-2(b) under the Securities Exchange Act of 1934. Yes ☐ No ☒

If ☒ is marked, indicate below the file number assigned to the registrant in connection with Rule 12g3-2(b): 82-

NEWS RELEASE

Havant, UK October 15, 2008 - Xyratex Ltd (Nasdaq: XRTX) today released the following financial information for the third quarter of its 2008 fiscal year, ending August 31, 2008:

- Management's Discussion and Analysis of Financial Condition and Results of Operations
- Unaudited condensed consolidated financial statements

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

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This section contains forward-looking statements. These statements relate to future events or our future financial performance and involve known and unknown risks, uncertainties and other factors that may cause our actual results, levels of activity, performance or achievements to differ materially from any future results, levels of activity, performance or achievements expressed or implied by these forward-looking statements. These risks and other factors include those listed under **Risk Factors** and elsewhere in our Annual Report on Form 20-F as filed with the Securities and Exchange Commission. In some cases, you can identify forward-looking statements by terminology such as **may**, **will**, **should**, **expects**, **intends**, **plans**, **anticipates**, **believes**, **estimates**, **predicts**, **potential**, **continue**, or the negative of these terms or other comparable terminology. Although we believe that the expectations reflected in the forward-looking statements are reasonable, we cannot guarantee future results, levels of activity, performance or achievements.

Overview

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We are a leading provider of modular enterprise-class data storage subsystems and storage process technology. We design, develop and manufacture enabling technology that provides our customers with data storage products to support high-performance storage and data communication networks. We operate in two business segments: Networked Storage Solutions and Storage Infrastructure.

Our Networked Storage Solutions products are primarily storage subsystems, which we provide to OEMs and our Storage Infrastructure products consist of disk drive manufacturing process equipment, which we sell directly to manufacturers of disk drives and disk drive components. We form long-term strategic relationships with our customers and we support them through our operations in the United States, Asia and Europe. In our 2007 fiscal year, sales to our top three customers, NetApp, Seagate Technology and Western Digital, accounted for 56%, 12% and 12% of our revenues, respectively. In the nine months ended August 31, 2008, sales to NetApp accounted for 56% of our revenues. No other customer accounted for more than 10% of our revenues in the period. We had 47 customers which individually contributed more than \$0.5 million to revenues in our 2007 fiscal year and at August 31, 2008 we had over 150 active customers. We enter into joint development projects with our key customers and suppliers in order to research and introduce new technologies and products.

Revenues

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Our Networked Storage Solutions products consist primarily of storage subsystems that address three market segments through our OEM customers: Network Attached Storage or NAS, Storage Area Networks or SAN, and Capacity Optimized storage. Our customers typically operate across multiple market segments. We have continued to see strong growth in each of these market segments over the past two fiscal years. Capacity Optimized storage is primarily driven by magnetic tape technology being replaced by storage systems containing low cost disk drive technology in the backup and recovery processes within enterprises. The deployment of low cost disk drives is also taking place within the SAN and NAS market segments as IT departments begin to classify their data as part of an information life cycle or corporate data management strategy. Our customers in each market segment currently use the Fibre Channel protocol to access the storage subsystem which can incorporate either high performance Fibre Channel or lower cost ATA/SATA disk drives.

Our Storage Infrastructure revenues are primarily derived from the sale of disk drive manufacturing process equipment directly to manufacturers of disk drives and disk drive components. We supply three main product lines in this segment: production test systems, servo track writers and media process technology (comprising media cleaning and media handling automation technology). Revenues from these products are subject to significant fluctuations, particularly from quarter to quarter, as they are dependent on the capital investment decisions and installation schedules of our customers.

We believe that both of our business segments present the opportunity for growth over the next several years. We have seen growth in demand from many of our customers, which we believe relates to factors including increases in the amount of digitally stored information, increased information technology spending, growth in the specific markets that our customers address, the trend towards outsourcing and increased market share of our customers. Growth in our Storage Infrastructure revenues can also be specifically affected by the growth in shipped volume and increases in the individual storage capacity of disk drives. Although we expect there to continue to be an underlying growth in demand for data storage, we would expect revenues over the next year to be impacted by the effects of upheaval in the financial markets on the macro-economic environment. In addition, commencing in 2009, we expect to enable our largest customer, NetApp, to source up to 25% of the products we supply from an alternative supplier. This will limit the opportunity to grow revenues in our Networked Storage Solutions segment.

The acquisition of Maxtor by Seagate Technology in May 2006 represented a significant consolidation among disk drive

suppliers and caused significant changes in market share. We believe these market share changes resulted in an exceptional level of purchases of our equipment in our 2006 fiscal year as our customers invested in new capacity to capture increased market share. In addition Seagate is reutilizing certain Maxtor-owned equipment, which was previously planned to be replaced by Xyratex equipment. This surplus capacity and reutilization of Maxtor owned equipment resulted in a significant decline in our revenues during 2007 fiscal year and the first half of our 2008 fiscal year when compared to our 2006 fiscal year. Revenues from our Storage Infrastructure products have begun to recover from the impact of these factors and we believe that the opportunity for growth in the longer term remains.

We typically enter into arrangements with our largest customers and provide them with products based on purchase orders executed under these arrangements. These arrangements often include estimates as to future product demand but do not typically specify minimum volume purchase requirements. Due to the complexity of our products, we provide almost all of our products on a build-to-order basis. The prices of our products are generally agreed to in advance and are based on a pre-negotiated pricing model. The pricing model may specify certain product components and component costs as well as anticipated profit margins.

As described above, the unit prices we obtain from our major customers will typically vary with volumes. As products become more mature, prices will generally decline, partly reflecting reduced component costs. We also regularly introduce new products which are likely to incorporate additional features or new technology and these products will generally command a higher unit price. Average unit prices will also vary with the mix of customers and products. Our unit prices for Networked Storage Solutions products have reduced in the last two fiscal years as volumes with our major customers have increased and prices are adjusted in line with the agreed price/volume matrix. Because this is related to volume growth, this has not resulted in a reduction in our revenues in those fiscal years and has also enabled reductions in component costs. With this exception, we have not seen an overall trend in our unit prices.

Foreign Exchange Rate Fluctuations

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The functional currency for all our operations is U.S. dollars and the majority of our revenues and cost of revenues are denominated in U.S. dollars. A significant proportion (approximately \$71.0 million in our 2007 fiscal year) of our non-U.S. dollar operating expenses relates to payroll and other expenses of our U.K. operations. To a lesser extent we are also exposed to movements in the Malaysian Ringgit relative to the U.S. dollar. We manage our exchange rate exposures through the use of forward foreign currency exchange contracts and option agreements. By using these derivative instruments, increases or decreases in our U.K. pound operating expenses resulting from changes in the U.S. dollar to U.K. pound exchange rate are partially offset by realized gains and losses on the derivative instruments.

Over our last three fiscal years there has been significant volatility in the exchange rate between the U.K. pound and the U.S. dollar. The effect of this volatility and movement is reduced because we have hedged the majority of our exposure to this exchange rate movement for approximately one year ahead. A 9% average decline in the value of the U.S. dollar in 2007 when compared to 2006 has increased our operating expenses by approximately \$4.0 million in our 2008 fiscal year, in comparison to our 2007 fiscal year. The dollar has subsequently risen in value by a similar amount and if this position is maintained this will reduce operating expenses in our 2009 fiscal year.

Costs of Revenues and Gross Profit

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Our costs of revenues consist primarily of the costs of the materials and components used in the assembly and manufacture of our products, including disk drives, electronic cards, enclosures and power supplies. Other items included in costs of revenues include salaries, bonuses and other labor costs for employees engaged in the component procurement, assembly and testing of our products, warranty expenses, shipping costs, depreciation of manufacturing equipment and certain overhead costs. Our gross margins change primarily as a result of fluctuations in our product mix. Our gross margins also change as a result of changes to product pricing, manufacturing volumes and costs of components. The gross margins for our Networked Storage Solutions products tend to be lower than the margins of our Storage Infrastructure products and therefore our gross profit as a percentage of revenues will continue to vary with the proportions of revenues in each segment.

Research and Development

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Our research and development expenses include expenses related to product development, engineering, materials costs and salaries, bonuses and other labor costs for our employees engaged in research and development. Research and development expenses include the costs incurred in designing products for our OEM customers, which often occurs prior to their commitment to purchase these products. We expense research and development costs as they are incurred.

Due to the level of competition in the markets in which we operate and the rapid changes in technology, our future revenues are heavily dependent on the improvements we make to our products and the introduction of new products. During our 2007 fiscal year our research and development expenses related to over approximately 45 separate projects covering improving existing products,

meeting customer specific requirements and entering new markets, such as development of the Storage Bridge Bay (SBB) compliant OneStor platform and the application of our media process automation technology to solar cell manufacturing.

As of November 2007, 26% of our employees were engaged in our research and development activities. Over recent fiscal years research and development expenses have risen approximately at the level of increase in revenue. Over the longer term we expect this trend to continue. In our 2007 fiscal year, although revenues declined, we continued to increase our research and development expenditure. This reflects our continuing commitment to developing products based on advanced technologies and designs to support growth in Networked Storage Solutions revenues and the longer term opportunities for growth of our Storage Infrastructure revenues.

Selling, General and Administrative

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Selling, general, and administrative expenses include expenses related to salaries, bonuses and other labor costs for senior management and sales, marketing, and administrative employees, market research and consulting fees, commissions to sales representatives, information technology costs, other marketing and sales activities and exchange gains and losses arising on the retranslation of U.K. pound denominated assets and liabilities. Our selling, general and administrative expenses have increased over recent fiscal years as we have grown our business. To the extent our business continues to grow we would expect these expenses to continue to increase approximately in line with our revenues.

Equity Compensation Expense

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We record equity compensation expense using the fair value method required by Financial Accounting Standard (FAS) 123R – Share Based Payment . Equity compensation expense calculated under FAS 123R for the nine month periods ended August 31, 2008 and August 31, 2007 was \$5.9 million and \$5.8 million respectively.

Equity Share Capital

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On January 14, 2008 we commenced a share buy-back program. We have announced that we will purchase our common shares up to a value of \$30 million and it is anticipated that the repurchase will take place over a period of up to one year. During the nine months ended August 31, 2008 we purchased 392,000 shares at a total value of \$6 million.

Provision for Income Taxes

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We are subject to taxation primarily in the United Kingdom, the United States and Malaysia. Our Malaysian operations benefit from a beneficial tax status which provided us with a zero tax rate on substantially all of our income arising in Malaysia. In 2006 we were granted a tax exempt status for substantially all of our operations in Malaysia until 2012, provided that we meet certain requirements. In the United Kingdom and the United States we benefit from research and development tax credits. As of November 30, 2007 we recorded a deferred tax asset of \$15.4 million related to loss carryforwards and other timing differences in the United Kingdom. The majority of this asset is denominated in U.K. pounds and income tax expense will therefore include exchange adjustments to this asset. As a result of loss carryforwards we have not been required to make any significant U.K. tax payments in recent fiscal years. Of the remaining deferred tax balance of \$7.3 million, \$5.3 million relates to equity compensation expense as described in the next paragraph and \$2.9 million relates to net operating loss carryforwards recorded in connection with our acquisition of nStor in 2005.

Following the introduction of FAS 123R in our 2006 fiscal year, we have recorded equity compensation expense using the fair value method. This has resulted in the recording of a tax benefit of \$3.5 million which is included in the deferred tax asset at November 30, 2007. We also recorded a deferred tax asset of \$1.8 million related to equity compensation expense calculated under the intrinsic method prior to our 2006 fiscal year. The realization of these elements of our deferred tax asset is dependent on future share price movements over the next four fiscal years. We anticipate recording any variation to the value of this asset as an adjustment to Additional Paid in Capital.

Tax payments in our 2007 fiscal year amounted to \$0.5 million and, due to the beneficial Malaysian tax status and U.K. tax losses, these tax payments related primarily to our U.S. operations. There has not been a significant change in the level of our tax payments in our 2008 fiscal year. Over the last three fiscal years our tax benefit or expense has primarily consisted of U.S. current taxes and movements in the U.K. deferred tax asset.

As described in the unaudited condensed consolidated financial statements, with effect from December 1, 2007, the Company adopted the provisions of FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an interpretation of FAS No. 109 (FIN 48). FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an entity s financial statements in

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accordance with FAS 109 and prescribes a recognition threshold and measurement attribute for financial statement disclosure of tax positions taken or expected to be taken on a tax return. As a result of the adoption of FIN 48, the Company recorded no additional unrecognized tax benefits. As of December 1, 2007, the Company had \$7.7 million of unrecognized tax benefits. If this asset were recognized approximately \$3.4 million would reduce our income tax expense and the remainder would result in a balance sheet reclassification only.

Results from Operations

The following table sets forth, for the periods indicated, selected operating data as a percentage of revenues.

	Three Months Ended August 31,		Nine Months Ended August 31,	
	2008	2007	2008	2007
Revenues	100.0%	100.0%	100.0%	100.0%
Cost of revenues	82.4	82.1	83.9	82.0
Gross profit	17.6	17.9	16.1	18.0
Operating expenses:				
Research and development	7.9	8.6	8.3	8.5
Selling, general and administrative	6.1	6.9	6.2	6.6
Amortization of intangible assets	0.4	0.6	0.5	0.7
Operating income	3.2	1.8	1.1	2.2
Net income	2.8	1.8	1.0	2.4
Segment gross profit as a percentage of segment revenues:				
Networked Storage Solutions	13.3	14.9	14.0	14.3
Storage Infrastructure	31.6	27.2	27.0	29.2

Three Months Ended August 31, 2008 Compared to Three Months Ended August 31, 2007

The following is a tabular presentation of our results of operations for the three months ended August 31, 2008 compared to the three months ended August 31, 2007. Following the table is a discussion and analysis of our business and results of operations for such periods.

	Three Months Ended		Increase / (Decrease)	
	August 31, 2008	August 31, 2007	Amount	%
US dollars in thousands				
Revenues:				
Networked Storage Solutions	\$ 213,100	\$ 174,004	\$ 39,096	22.5%
Storage Infrastructure	67,680	60,210	7,470	12.4
Total revenues	280,780	234,214	46,566	19.9
Cost of revenues	231,293	192,274	39,019	20.3
Gross profit:				
Networked Storage Solutions	28,401	25,847	2,554	9.9
Storage Infrastructure	21,386	16,403	4,983	30.4
Equity compensation	(300)	(310)	(10)	
Total gross profit	49,487	41,940	7,547	18.0

Operating expenses:

Research and development