

KRATOS DEFENSE & SECURITY SOLUTIONS, INC.

Form 10-Q

November 07, 2014

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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 September 28, 2014

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

Commission file number 001-34460

KRATOS DEFENSE & SECURITY SOLUTIONS, INC.

(Exact name of Registrant as specified in its charter)

Delaware

13-3818604

(State or other jurisdiction of incorporation or organization)

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

4820 Eastgate Mall, Suite 200

San Diego, CA 92121

(858) 812-7300

(Address, including zip code, and telephone number, including area code, of Registrant's principal executive offices)

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (Section 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 the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act:

Large accelerated filer

Accelerated filer

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

As of October 31, 2014, 57,796,295 shares of the registrant's common stock were outstanding.

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FORM 10-Q

FOR THE QUARTERLY PERIOD ENDED September 28, 2014

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements.

KRATOS DEFENSE & SECURITY SOLUTIONS, INC.
 CONDENSED CONSOLIDATED BALANCE SHEETS
 (in millions, except par value and number of shares)
 (Unaudited)

	December 29, 2013	September 28, 2014
Assets		
Current assets:		
Cash and cash equivalents	\$55.7	\$16.2
Restricted cash	5.0	5.2
Accounts receivable, net	265.8	255.1
Inventoried costs	74.6	80.4
Prepaid expenses	10.4	9.0
Other current assets	18.8	10.8
Total current assets	430.3	376.7
Property, plant and equipment, net	84.8	82.6
Goodwill	596.4	596.4
Intangible assets, net	69.9	57.8
Other assets	35.2	32.4
Total assets	\$1,216.6	\$1,145.9
Liabilities and Stockholders' Equity		
Current liabilities:		
Accounts payable	\$61.9	\$49.2
Accrued expenses	46.2	37.0
Accrued compensation	44.9	37.1
Accrued interest	5.2	16.7
Billings in excess of costs and earnings on uncompleted contracts	52.5	47.2
Deferred income tax liability	28.4	28.4
Other current liabilities	11.9	11.6
Total current liabilities	251.0	227.2
Long-term debt principal, net of current portion	628.8	621.9
Long-term debt premium	14.5	—
Line of credit	—	41.0
Other long-term liabilities	26.5	24.8
Total liabilities	920.8	914.9
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$0.001 par value, 5,000,000 shares authorized, 0 shares outstanding at December 29, 2013 and September 28, 2014	—	—
Common stock, \$0.001 par value, 195,000,000 shares authorized; 57,056,892 and 57,795,095 shares issued and outstanding at December 29, 2013 and September 28, 2014, respectively	—	—
Additional paid-in capital	856.0	867.2
Accumulated other comprehensive loss	(0.8	) (1.0
Accumulated deficit	(559.4	) (635.2
Total stockholders' equity	295.8	231.0

Total liabilities and stockholders' equity	\$1,216.6	\$1,145.9
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The accompanying notes are an integral part of these condensed consolidated financial statements.

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KRATOS DEFENSE & SECURITY SOLUTIONS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)

(in millions, except per share amounts)

(Unaudited)

	Three Months Ended		Nine Months Ended	
	September 29, 2013	September 28, 2014	September 29, 2013	September 28, 2014
Service revenues	\$108.8	\$97.1	\$335.0	\$299.5
Product sales	117.6	120.0	379.9	347.0
Total revenues	226.4	217.1	714.9	646.5
Cost of service revenues	82.4	77.7	254.3	229.7
Cost of product sales	91.7	86.4	282.1	254.8
Total costs	174.1	164.1	536.4	484.5
Gross profit	52.3	53.0	178.5	162.0
Selling, general and administrative expenses	47.8	45.8	144.9	134.1
Merger and acquisition expenses	0.2	—	(2.3) —
Research and development expenses	4.8	5.9	14.5	17.0
Unused office space and other restructuring	(6.6	) 0.1	(5.0	) 1.7
Operating income from continuing operations	6.1	1.2	26.4	9.2
Other income (expense):				
Interest expense, net	(16.2	) (12.1	) (48.7	) (42.2
Loss on extinguishment of debt	—	—	—	(39.1
Other income (expense), net	0.8	(0.4	) 0.2	—
Total other expense, net	(15.4	) (12.5	) (48.5	) (81.3
Loss from continuing operations before income taxes	(9.3	) (11.3	) (22.1	) (72.1
Provision (benefit) for income taxes from continuing operations	0.2	(0.2	) 2.9	3.7
Loss from continuing operations	(9.5	) (11.1	) (25.0	) (75.8
Income (loss) from discontinued operations	(0.4	) 0.2	(4.8) —
Net loss	\$(9.9	) \$(10.9	) \$(29.8	) \$(75.8
Basic and diluted loss per common share:				
Net loss from continuing operations	\$(0.17	) \$(0.19	) \$(0.44	) \$(1.32
Net loss from discontinued operations	0.00	0.00	(0.08	) 0.00
Net loss per common share	\$(0.17	) \$(0.19	) \$(0.52	) \$(1.32
Basic and diluted weighted average shares outstanding	57.1	57.8	56.7	57.6
Comprehensive Loss				
Net loss from above	\$(9.9	) \$(10.9	) \$(29.8	) \$(75.8
Change in cumulative translation adjustment	(0.1	) (0.1	) —	(0.2
Comprehensive loss	\$(10.0	) \$(11.0	) \$(29.8	) \$(76.0

The accompanying notes are an integral part of these condensed consolidated financial statements.

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KRATOS DEFENSE & SECURITY SOLUTIONS, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (in millions)
 (Unaudited)

	Nine Months Ended September 29, 2013	September 28, 2014
Operating activities:		
Net loss	\$(29.8	) \$(75.8
Less: Loss from discontinued operations	(4.8) —
Loss from continuing operations	(25.0	) (75.8
Adjustments to reconcile loss from continuing operations to net cash provided by (used in) operating activities from continuing operations:		
Depreciation and amortization	40.7	29.2
Stock-based compensation	6.0	7.6
Amortization of deferred financing costs	3.9	2.5
Amortization of premium and discount on Senior Secured Notes	(3.1	) (1.1
Loss on extinguishment of debt	—	39.1
Provision for doubtful accounts	0.8	1.2
Changes in unused office space accrual	(6.8	) 0.2
Changes in assets and liabilities, net of acquisitions:		
Accounts receivable	2.1	9.6
Inventoried costs	10.9	(6.0
Prepaid expenses and other assets	0.3	0.8
Accounts payable	(26.1	) (12.7
Accrued compensation	(10.8	) (7.8
Accrued expenses	(1.5	) (9.2
Accrued interest payable	15.6	11.5
Billings in excess of costs and earnings on uncompleted contracts	7.5	(7.4
Income tax receivable and payable	3.9	2.1
Other liabilities	(7.4	) (2.0
Net cash provided by (used in) operating activities from continuing operations	11.0	(18.2
Investing activities:		
Cash paid for acquisitions, net of cash acquired	2.2	(2.6
Proceeds from the sale of discontinued operations	0.4	—
Increase (decrease) in restricted cash	0.5	(0.1
Capital expenditures	(12.2	) (9.4
Net cash used in investing activities from continuing operations	(9.1	) (12.1
Financing activities:		
Proceeds from issuance of long-term debt	—	618.5
Extinguishment of long-term debt	—	(661.5
Debt issuance costs	—	(8.5
Credit agreement borrowings	—	41.0
Cash paid for contingent acquisition consideration	(2.1) —
Repayment of debt	(0.8	) (0.7
Other	1.2	3.3
Net cash used in financing activities from continuing operations	(1.7	) (7.9
Net cash flows of continuing operations	0.2	(38.2