

UFP TECHNOLOGIES INC
Form 10-Q
November 07, 2014
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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 SEPTEMBER 30, 2014

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: 001-12648

UFP Technologies, Inc.

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(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

04-2314970

(IRS Employer Identification No.)

172 East Main Street, Georgetown, Massachusetts 01833, USA

(Address of principal executive offices) (Zip Code)

(978) 352-2200

(Registrant's telephone number, including area code)

(Former name, former address, and former fiscal year, if changed since last report)

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 x; No o

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, 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 x; No o

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. (Check one):

| | |
|---------------------------|---|
| Large accelerated filer | <input type="radio"/> |
| Accelerated filer | <input checked="" type="radio"/> |
| Non-accelerated filer | <input type="radio"/> [Do not check if a smaller reporting company] |
| Smaller reporting company | <input type="radio"/> |

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o; No x

7,056,569 shares of registrant's Common Stock, \$0.01 par value, were outstanding as of November 3, 2014.

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UFP Technologies, Inc.

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Table of Contents**PART I: FINANCIAL INFORMATION****ITEM 1: FINANCIAL STATEMENTS****UFP Technologies, Inc.****Condensed Consolidated Balance Sheets**

(In thousands, except share data)

| | September 30, 2014 (Unaudited) | December 31, 2013 |
|--|--------------------------------------|----------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 33,048 | \$ 37,303 |
| Receivables, less allowance for doubtful accounts of \$529 at September 30, 2014 and \$512 at December 31, 2013 | 18,565 | 17,032 |
| Inventories | 13,500 | 11,048 |
| Prepaid expenses | 947 | 690 |
| Refundable income taxes | 829 | 1,537 |
| Deferred income taxes | 1,284 | 1,222 |
| Total current assets | 68,173 | 68,832 |
| Property, plant, and equipment | 74,336 | 64,574 |
| Less accumulated depreciation and amortization | (40,797) | (39,067) |
| Net property, plant, and equipment | 33,539 | 25,507 |
| Goodwill | 7,322 | 7,322 |
| Intangible assets, net | 1,033 | 1,346 |
| Other assets | 2,071 | 2,013 |
| Total assets | \$ 112,138 | \$ 105,020 |
| Liabilities and Stockholders Equity | | |
| Current liabilities: | | |
| Accounts payable | \$ 5,269 | \$ 3,081 |
| Accrued expenses | 7,001 | 8,265 |
| Current installments of long-term debt | 989 | 976 |
| Total current liabilities | 13,259 | 12,322 |
| Long-term debt, excluding current installments | 2,123 | 2,867 |
| Deferred income taxes | 2,151 | 2,436 |
| Retirement and other liabilities | 1,602 | 1,805 |
| Total liabilities | 19,135 | 19,430 |
| Commitments and contingencies | | |
| Stockholders equity: | | |
| Preferred stock, \$.01 par value. Authorized 1,000,000 shares; zero shares issued or outstanding | | |
| Common stock, \$.01 par value. Authorized 20,000,000 shares; issued and outstanding 7,056,569 at September 30, 2014 and 6,900,683 at December 31, 2013 | 71 | 69 |
| Additional paid-in capital | 21,714 | 20,291 |

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| | | |
|--|------------|------------|
| Retained earnings | 71,218 | 65,230 |
| Total stockholders' equity | 93,003 | 85,590 |
| Total liabilities and stockholders' equity | \$ 112,138 | \$ 105,020 |

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

Table of Contents**UFP Technologies, Inc.****Condensed Consolidated Statements of Income**

(In thousands, except per share data)

(Unaudited)

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|-------------------------------------|-----------|------------------------------------|------------|
| | 2014 | 2013 | 2014 | 2013 |
| Net sales | \$ 35,406 | \$ 34,700 | \$ 104,040 | \$ 104,229 |
| Cost of sales | 25,723 | 24,538 | 75,773 | 74,445 |
| Gross profit | 9,683 | 10,162 | 28,267 | 29,784 |
| Selling, general & administrative expenses | 5,871 | 5,678 | 18,161 | 17,700 |
| Restructuring costs | 772 | | 1,096 | |
| (Gain) loss on sale of fixed assets | (58) | | (70) | 11 |
| Operating income | 3,098 | 4,484 | 9,080 | 12,073 |
| Interest expense, net | (20) | (43) | (69) | (128) |
| Other income, net | 101 | | 201 | |
| Income before income tax expense | 3,179 | 4,441 | 9,212 | 11,945 |
| Income tax expense | 1,113 | 1,554 | 3,224 | 4,046 |
| Net income | \$ 2,066 | \$ 2,887 | \$ 5,988 | \$ 7,899 |
| <i>Net income per share:</i> | | | | |
| Basic | \$ 0.29 | \$ 0.42 | \$ 0.85 | \$ 1.16 |
| Diluted | \$ 0.29 | \$ 0.41 | \$ 0.84 | \$ 1.11 |
| <i>Weighted average common shares outstanding:</i> | | | | |
| Basic | 7,055 | 6,840 | 7,018 | 6,802 |
| Diluted | 7,186 | 7,112 | 7,170 | 7,096 |

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

Table of Contents**UFP Technologies, Inc.****Condensed Consolidated Statements of Cash Flows**

(In thousands)

(Unaudited)

| | Nine Months Ended September 30, | |
|---|--|------------------|
| | 2014 | 2013 |
| Cash flows from operating activities: | | |
| Net income | \$ 5,988 | \$ 7,899 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 3,207 | 2,982 |
| (Gain) loss on sale of fixed assets | (70) | 11 |
| Share-based compensation | 945 | 707 |
| Excess tax benefit on share-based compensation | (845) | (7) |
| Deferred income taxes | (347) | (11) |
| Changes in operating assets and liabilities: | | |
| Receivables, net | (1,533) | 30 |
| Inventories | (2,452) | (202) |
| Prepaid expenses | (257) | (274) |
| Refundable income taxes | 1,553 | 1,714 |
| Other assets | (58) | (236) |
| Accounts payable | 2,188 | (529) |
| Accrued taxes and other expenses | (1,264) | (786) |
| Retirement and other liabilities | (203) | 242 |
| Net cash provided by operating activities | 6,852 | 11,540 |
| Cash flows from investing activities: | | |
| Additions to property, plant, and equipment | (10,940) | (5,017) |
| Holdback payment related to the acquisition of Packaging Alternatives Corporation | | (600) |
| Redemption of cash value life insurance | | 37 |
| Proceeds from sale of fixed assets | 84 | 1 |
| Net cash used in investing activities | (10,856) | (5,579) |
| Cash flows from financing activities: | | |
| Proceeds from the issuance of long-term debt | | 580 |
| Principal repayments of long-term debt | (731) | (1,156) |
| Proceeds from exercise of stock options, net of attestation | 336 | 335 |
| Excess tax benefit on share-based compensation | 845 | 7 |
| Payment of statutory withholdings for stock options exercised and restricted stock units vested | (701) | (974) |
| Net cash used in financing activities | (251) | (1,208) |
| Net (decrease) increase in cash and cash equivalents | (4,255) | 4,753 |
| Cash and cash equivalents at beginning of period | 37,303 | 33,480 |
| Cash and cash equivalents at end of period | \$ 33,048 | \$ 38,233 |

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

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Notes to Interim Condensed Consolidated Financial Statements

(1) Basis of Presentation

The interim condensed consolidated financial statements of UFP Technologies, Inc. (the Company) presented herein, have been prepared pursuant to the rules of the Securities and Exchange Commission for quarterly reports on Form 10-Q and do not include all the information and note disclosures required by accounting principles generally accepted in the United States of America. These statements should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2013, included in the Company's 2013 Annual Report on Form 10-K as filed with the Securities and Exchange Commission.

The condensed consolidated balance sheet as of September 30, 2014, the condensed consolidated statements of income for the three- and nine-month periods ended September 30, 2014, and 2013, and the condensed consolidated statements of cash flows for the nine-month periods ended September 30, 2014, and 2013 are unaudited but, in the opinion of management, include all adjustments (consisting of normal, recurring adjustments) necessary for a fair presentation of results for these interim periods.

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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 revenues and expenses during the reporting period.

The results of operations for the three- and nine-month periods ended September 30, 2014, are not necessarily indicative of the results to be expected for the entire fiscal year ending December 31, 2014.

(2) Supplemental Cash Flow Information

Cash paid for interest and income taxes is as follows (in thousands):

| | Nine Months Ended September 30, | | | |
|------------------------------|--|-------|-------------|-------|
| | 2014 | | 2013 | |
| Interest | \$ | 72 | \$ | 129 |
| Income taxes, net of refunds | \$ | 2,019 | \$ | 2,027 |

During the nine-month periods ended September 30, 2014, and 2013, the Company permitted the exercise of stock options with exercise proceeds paid with the Company's stock (cashless exercises) totaling approximately \$372,000 and \$225,000, respectively.

(3) Fair Value Accounting

The Company has financial instruments, such as accounts receivable, accounts payable, and accrued expenses, which are stated at carrying amounts that approximate fair value because of the short maturity of those instruments. The carrying amount of the Company's long-term debt approximates fair value as the interest rate on the debt approximates the estimated borrowing rate currently available to the Company.

(4) Share-Based Compensation

Share-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as an expense over the requisite service period (generally the vesting period of the equity grant).

The Company issues share-based awards through several plans that are described in detail in the notes to the consolidated financial statements for the year ended December 31, 2013. The compensation cost charged against income for those plans is included in selling, general & administrative expenses as follows (in thousands):

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| | Three Months Ended September 30, | | | | Nine Months Ended September 30, | | | |
|--|-------------------------------------|-----|------|-----|------------------------------------|-----|------|-----|
| | 2014 | | 2013 | | 2014 | | 2013 | |
| Total share-based compensation expense | \$ | 215 | \$ | 200 | \$ | 945 | \$ | 707 |

Share-based compensation for the nine-month periods ended September 30, 2014 and 2013 includes approximately \$128,000 and \$60,000, respectively, representing the fair value of the Company's common stock granted during the period to the Board of Directors.

The total income tax benefit recognized in the condensed consolidated statements of income for share-based compensation arrangements was approximately \$60,000 and \$58,000 for the three-month periods ended September 30, 2014, and 2013, respectively, and \$276,000 and \$215,000 for the nine-month periods ended September 30, 2014, and 2013, respectively.

The following is a summary of stock option activity under all plans for the nine-month period ended September 30, 2014:

| | Shares Under Options | Weighted Average Exercise Price (per share) | Weighted Average Remaining Contractual Life (in years) | Aggregate Intrinsic Value (in thousands) |
|---|-------------------------|--|---|---|
| Outstanding at December 31, 2013 | 467,500 | \$ 9.00 | | |
| Granted | 35,193 | 24.69 | | |
| Exercised | (162,586) | 4.36 | | |
| Outstanding at September 30, 2014 | 340,107 | \$ 12.84 | 4.08 | \$ 3,204 |
| Exercisable at September 30, 2014 | 257,608 | \$ 10.35 | 4.17 | \$ 3,044 |
| Vested and expected to vest at September 30, 2014 | 340,107 | \$ 12.84 | 4.08 | \$ 3,204 |

On March 12, 2014, the Company granted one of its directors options to purchase 577 shares of its common stock at that day's closing price of \$25.48. On June 11, 2014, the Company granted options to certain employees and directors for the purchase of 15,000 shares and 14,616 shares, respectively, of common stock at that day's closing price of \$25.04. On September 10, 2014, the Company granted options to certain employees for the purchase of 5,000 shares of common stock at that day's closing price of \$22.55. The compensation expense related to these grants was determined as the fair value of the options using the Black Scholes option pricing model based on the following assumptions:

| | |
|-------------------------|------------------|
| Expected volatility | 32.3% to 37.9% |
| Expected dividends | None |
| Risk free interest rate | 0.7% to 0.9% |
| Expected term | 3.8 to 5.0 years |

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The stock volatility for each grant is determined based on a review of the experience of the weighted average of historical daily price changes of the Company's common stock over the expected option term, and the risk-free rate is based on the U.S. Treasury yield curve in effect at the time of grant for periods corresponding with the expected life of the option. The expected term of the Company's options is determined using a simplified method based on the average of the weighted vesting terms and the contractual term of the options. The weighted average grant date fair value of options granted during the nine-month period ended September 30, 2014 was \$7.24.

During the nine-month periods ended September 30, 2014, and 2013, the total intrinsic value of all options exercised (i.e., the difference between the market price on the exercise date and the price paid by the employees to exercise the options) was approximately \$3.4 million and \$2.0 million, respectively, and the total amount of consideration received by the Company from the exercised options was approximately \$709,000

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and \$334,000, respectively. At its discretion, the Company allows option holders to surrender previously owned common stock in lieu of paying the exercise price and withholding taxes. During the nine-months ended September 30, 2014, 32,164 shares (14,931 for options and 17,233 for taxes) were surrendered at an average market price of \$25.42.

During the three-month periods ended September 30, 2014, and 2013, the Company recognized compensation expenses related to stock options granted to directors and employees of approximately \$44,000 and \$40,000, respectively. During the nine-month periods ended September 30, 2014, and 2013, the Company recognized compensation expenses related to stock options granted to directors and employees of approximately \$310,000 and \$165,000, respectively.

On February 18, 2014, the Company's Compensation Committee approved the award of \$400,000, payable in shares of common stock to the Company's Chairman, Chief Executive Officer, and President under the 2003 Incentive Plan. The shares will be issued on or before December 31, 2014. The Company recorded compensation expense associated with the award of \$100,000 and \$300,000, respectively, during both the three- and nine-month periods ended September 30, 2014 and 2013.

The following table summarizes information about Restricted Stock Units (RSUs) activity during the nine-month period ended September 30, 2014:

| | Restricted Stock Units | Weighted Average Award Date Fair Value |
|--------------------------------|---------------------------|--|
| Unvested at December 31, 2013 | 50,900 | \$ 11.94 |
| Awarded | 22,338 | 25.94 |
| Shares vested | (30,253) | 10.11 |
| Unvested at September 30, 2014 | 42,985 | \$ 18.59 |

During the three- and nine-month periods ended September 30, 2014, the Company recorded compensation expense related to RSUs of approximately \$71,000 and \$207,000, respectively. The Company recorded compensation expense of approximately \$60,000 and \$182,000, respectively, for the same periods of 2013.

At the Company's discretion, RSU holders are given the option to net-share settle to cover the required minimum withholding tax, and the remaining amount is converted into the equivalent number of common shares. During the nine-month periods ended September 30, 2014 and 2013, 9,878 and 37,796 shares were surrendered at an average market price of \$25.88 and \$19.81, respectively.

At September 30, 2014, the company had approximately \$915,000 of unrecognized compensation expense, which is expected to be recognized over a period of 3.75 years.

(5) **Inventories**

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Inventories are stated at the lower of cost (first-in, first-out) or market, and consist of the following at the stated dates (in thousands):

| | September 30, 2014 | | December 31, 2013 | |
|-----------------|-----------------------|--------|----------------------|--------|
| Raw materials | \$ | 8,685 | \$ | 6,627 |
| Work in process | | 1,278 | | 1,056 |
| Finished goods | | 3,537 | | 3,365 |
| Total inventory | \$ | 13,500 | \$ | 11,048 |

Table of Contents**(6) Preferred Stock**

On March 18, 2009, the Company declared a dividend of one preferred share purchase right (a Right) for each outstanding share of common stock, par value \$0.01 per share, to the stockholders of record on March 20, 2009. Each Right entitles the registered holder to purchase from the Company one one-thousandth of a share of Series A Junior Participating Preferred Stock, par value \$0.01 per share (the Preferred Share) of the Company, at a price of \$25 per one one-thousandth of a Preferred Share subject to adjustment and the terms of the Rights Agreement. The Rights expire on March 19, 2019.

(7) Income Per Share

Basic income per share is based on the weighted average number of shares of common stock outstanding. Diluted income per share is based upon the weighted average number of common shares outstanding and dilutive common stock equivalent shares outstanding during each period.

The weighted average number of shares used to compute basic and diluted net income per share consisted of the following (in thousands):

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|--|-------------------------------------|-------|------------------------------------|-------|
| | 2014 | 2013 | 2014 | 2013 |
| Weighted average common shares outstanding, basic | 7,055 | 6,840 | 7,018 | 6,802 |
| Weighted average common equivalent shares due to stock options and RSUs | 131 | 272 | 152 | 294 |
| Weighted average common shares outstanding, diluted | 7,186 | 7,112 | 7,170 | 7,096 |

The computation of diluted earnings per share excludes the effect of the potential exercise of stock awards, including stock options, when the average market price of the common stock is lower than the exercise price of the related options during the period. These outstanding stock awards are not included in the computation of diluted income per share because the effect would be antidilutive. For both the three- and nine-month periods ended September 30, 2014, the number of stock awards excluded from the computation of diluted earnings per share was 53,651. For the three- and nine-month periods ended September 30, 2013, the number of stock awards excluded from the computation of diluted earnings per share was 71,546 and 88,908, respectively.

(8) Segment Reporting

The Company has historically reported two segments, Component Products and Packaging. However, the Company has been undergoing a shift in the way the business is managed and the way information is used by the Chief Operating Decision Maker (the CODM), who is the Chief Executive Officer, to consider risks and opportunities and to make decisions and review performance as further described below. In late 2013 and into 2014 the Company committed to changes to the Company's operations including plant consolidations, consolidation of the Company's

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sales force, and other strategic initiatives, to coincide with the Company's change in operating strategy to maximize capacity in each plant and enhance customer service across markets. By the end of the third quarter of 2014, many of those initiatives were complete and the Company determined that the existing segment aggregation of Component Products and Packaging was no longer consistent with how the business is structured and reviewed by the CODM. This is primarily because the Company has numerous manufacturing processes that are duplicated through its plants allowing it to move workload based on available capacity and proximity to customers. The CODM evaluates consolidated financial information to manage the business. As a result, the Company has determined that it consists of a single operating and reportable segment.

Revenues from customers outside of the United States are not material. No customer comprised more than 10% of the Company's consolidated revenues for the three- and nine-month periods ended September 30, 2014. All of the Company's assets are located in the United States.

Table of Contents**(9) Other Intangible Assets**

The carrying values of the company's definite lived intangible assets as of September 30, 2014, and December 31, 2013, are as follows (in thousands):

| | Patents | Non-Compete | Customer List | Total |
|--|----------------|--------------------|----------------------|--------------|
| Estimated useful life | 14 years | 5 years | 5 years | |
| Gross amount at September 30, 2014 | \$ 429 | \$ 512 | \$ 2,046 | \$ 2,987 |
| Accumulated amortization at September 30, 2014 | (429) | (309) | (1,216) | (1,954) |
| Net balance at September 30, 2014 | \$ | \$ 203 | \$ 830 | \$ 1,033 |
| Gross amount at December 31, 2013 | \$ 429 | \$ 512 | \$ 2,046 | \$ 2,987 |
| Accumulated amortization at December 31, 2013 | (429) | (249) | (963) | (1,641) |
| Net balance at December 31, 2013 | \$ | \$ 263 | \$ 1,083 | \$ 1,346 |

Amortization expense related to intangible assets was approximately \$81,000 and \$119,000 for the three-month periods ended September 30, 2014, and 2013, respectively, and \$313,000 and \$358,000 for the nine-month periods ended September 30, 2014, and 2013. The estimated remaining amortization expense as of September 30, 2014 is as follows (in thousands):

| | |
|---------------|----------|
| Remainder of: | |
| 2014 | \$ 79 |
| 2015 | 318 |
| 2016 | 318 |
| 2017 | 318 |
| Total | \$ 1,033 |

(10) Income Taxes

The income tax expense included in the accompanying unaudited consolidated statements of income principally relates to the Company's proportionate share of the pre-tax income of its wholly-owned subsidiaries. The determination of income tax expense for interim reporting purposes is based upon the estimated effective tax rate for the year, adjusted for the impact of any discrete items which are accounted for in the period in which they occur.

The Company recorded a tax expense of approximately 35.0% of income before income tax expense for the three-month periods ended September 30, 2014, and 2013, respectively. The Company recorded a tax expense of approximately 35.0% of income before income tax expense for the nine-month period ended September 30, 2014, compared to a tax expense of approximately 33.9% for the comparable nine-month period in 2013. The increase in the effective tax rate was a result of a retroactive application for a 2012 research and development credit which was recorded as a discrete event in the first quarter of 2013. Excluding this discrete event, the effective tax rate for the nine months ended September 30, 2013, was also approximately 35.0%.

(11) Plant Consolidations

On January 7, 2014, the Company committed to move forward with a plan to cease operations at its Glendale Heights, Illinois plant and consolidate operations into its Grand Rapids, Michigan, facility. The Company's decision was in response to a pending significant increase in lease cost, declining sales at the Illinois facility, and significant anticipated savings as a result of the consolidation. The Company expects annual cost savings of approximately \$750,000 as a result of the Michigan plant consolidation. The consolidation into the Michigan

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facility is substantially complete and the actual costs incurred through September 30, 2014 are included in the table below.

On July 16, 2014, the Company committed to move forward with a plan to cease operations at its Costa Mesa, California, plant and consolidate operations into its Rancho Dominguez, California, facility and other UFP facilities. The Company's decision was in response to the upcoming December 31, 2014, expiration of the lease on the Costa Mesa facility as well as the close proximity of the two properties. The Company expects the activities related to this consolidation to be completed on or before December 31, 2014.

The Company expects to incur approximately \$535,000 in one-time expenses in connection with the consolidation of the California plants. Included in the \$535,000 amount are approximately \$50,000 of expenses the Company expects to incur relating to employee severance payments, approximately \$465,000 in moving expenses and expenses associated with vacating the Costa Mesa property and approximately \$20,000 in expenses in moving equipment within the Rancho Dominguez location. The Company does not expect to incur any lease separation costs as the completion of the move is expected to coincide with the expiration of the Costa Mesa lease. Total cash charges are estimated at \$535,000 and the actual costs incurred through September 30, 2014 are included in the table below. The Company expects annual cost savings of approximately \$550,000 as a result of the California plant consolidation.

The Company has recorded the following restructuring costs associated with the plant consolidations discussed above for the three and nine-month periods ended September 30, 2014 (in thousands):

| Restructuring Costs | Three Months Ended September 30, 2014 | | | Nine Months Ended September 30, 2014 | | |
|-----------------------------|--|------------|--------|---|------------|----------|
| | Michigan | California | Total | Michigan | California | Total |
| Employee severance payments | \$ 212 | \$ | \$ 212 | \$ 237 | \$ | \$ 237 |
| Relocation costs | 241 | 62 | 303 | 356 | 62 | 418 |
| Workforce training costs | 249 | | 249 | 362 | | 362 |
| Plant infrastructure costs | 8 | | 8 | 79 | | 79 |
| Total restructuring costs | \$ 710 | \$ 62 | \$ 772 | \$ 1,034 | \$ 62 | \$ 1,096 |

The Company also incurred approximately \$219,000 and \$350,000 for the three- and nine-month periods ended September 30, 2014, respectively, in related capital improvements at its Michigan facility.

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ITEM 2: MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-looking Statements

This report contains certain statements that are forward-looking statements as that term is defined under the Private Securities Litigation Reform Act of 1995 and releases issued by the Securities and Exchange Commission. The words believe, expect, anticipate, intend, plan, estimate, and other expressions, which are predictions of or indicate future events and trends and that do not relate to historical matters, identify forward-looking statements. Examples of forward-looking statements included in this report include, without limitation, statements regarding the anticipated financial performance and/or future business prospects of the Company, anticipated trends in the different markets in which the Company competes, expectations regarding the Company's results of operations, financial condition and the sufficiency of the Company's capital resources, statements regarding the Company's capital expenditure plans and expansion of our business and anticipated advantages associated therewith, including the development of and investments in its molded fiber product line, expectations regarding the manufacturing capacity and efficiencies of the Company's production equipment, anticipated advantages relating to the Company's decisions to consolidate its Midwest and California facilities and the expected costs, savings and efficiencies associated therewith, expected methods of growth for the Company, expectations regarding the Company's acquisition strategy, any indication that the Company may be able to sustain or increase its sales and earnings or sales and earnings growth rates and statements regarding the overall economy.

Forward-looking statements involve known and unknown risks, uncertainties and other factors, which may cause the actual results, performance, or achievements of the Company to differ materially from anticipated future results, performance, or achievements expressed or implied by such forward-looking statements. Examples of these risks, uncertainties, and other factors include, without limitation, the following: economic conditions that affect sales of the products of the Company's customers, risks associated with the identification of suitable acquisition candidates and the successful, efficient execution and integration of such acquisitions, the implementation of new production equipment in a timely, cost-efficient manner, risks that any benefits from such new equipment may be delayed or not fully realized, or that the Company may be unable to fully utilize its production capacity, actions by the Company's competitors, and the ability of the Company to respond to such actions, the ability of the Company to obtain new customers, the ability of the Company to offset lost revenues, evolving customer requirements, difficulties associated with the roll-out of new products, decisions by customers to cancel or defer orders for the Company's products that previously had been accepted, risks and uncertainties associated with plant closures and expected efficiencies from consolidating manufacturing, the costs of compliance with the requirements of Sarbanes-Oxley, and general economic and industry conditions and other factors. In addition to the foregoing, the Company's actual future results could differ materially from those projected in the forward-looking statements as a result of the risk factors set forth elsewhere in this report and changes in general economic conditions, interest rates and the assumptions used in making such forward-looking statements. All of the forward-looking statements are qualified in their entirety by reference to the risk factors and other disclaimers described in the Company's filings with the Securities and Exchange Commission, in particular its most recent Annual Report on Form 10-K. The Company undertakes no obligation to publicly update or revise any forward-looking statement, whether as a result of new information, future events or otherwise.

Unless the context requires otherwise, the terms *we*, *us*, *our*, or *the Company* refer to UFP Technologies, Inc. and its consolidated subsidiaries.

Overview

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Using foams, plastics, composites, and natural fiber materials, UFP Technologies designs and manufactures a vast range of solutions primarily for the medical, aerospace and defense, automotive, and packaging markets.

During the third quarter of 2014, in conjunction with the consolidation of operations in Michigan and the consolidation of the Company's sales force, the Company determined that the existing segment aggregation of Component Products and Packaging was no longer consistent with how the business is structured and reviewed by the Chief Operating Decision Maker (the CODM). This is primarily because the Company has numerous manufacturing processes that are duplicated through its plants allowing it to move workload based on available capacity and proximity to customers. The CODM evaluates consolidated financial information to manage the business. As a result, the Company has determined that it consists of a single operating and reportable segment.

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The Company realized a 0.2% decrease in year-to-date sales through September 30, 2014, compared to the same period in 2013, largely due to a 6% reduction in sales to the automotive market partially offset by an increase of 3% in sales to the medical market. This decline in sales, combined with higher overhead costs and approximately \$1.1 million in restructuring costs resulted in a 24.8% decrease in operating income for the nine-month period ended September 30, 2014. The Company expects to incur additional restructuring charges in the fourth quarter of 2014 associated with the previously announced plant consolidation in California.

The Company's current strategy includes organic growth and growth through strategic acquisitions.

Results of Operations

Sales

Sales for the three-month period ended September 30, 2014, increased approximately 2.0% to \$35.4 million from sales of \$34.7 million for the same period in 2013. Sales for the nine-month period ended September 30, 2014, decreased approximately 0.2% to \$104.0 million from sales of \$104.2 million for the same period in 2013. The increase in sales for the three-month period ended September 30, 2014, is primarily due to an increase in sales to the aerospace and defense market of approximately 60% primarily due to a large one-time order from a defense contractor as well as an increase in orders for soldiers uniform and equipment components and increased sales to the medical market of approximately 4%, partially offset by a 14% decline in sales to the automotive market due largely to the phase-out of a mid-west program and soft demand for interior trim components. In the absence of the large one-time order, sales to the aerospace and defense market increased approximately 29% for the three-month period ended September 30, 2014. The slight decrease in sales for the nine-month period ended September 30, 2014, is primarily due to a 6% decline in sales to the automotive market due largely to soft demand for interior trim components, partially offset by increased sales to the medical market of approximately 3%.

Gross Profit

Gross profit as a percentage of sales (gross margin) decreased to 27.3% for the three-month period ended September 30, 2014, from 29.3% for the same period in 2013. This decrease is primarily due to higher employee health care costs and other fringe benefits of approximately \$430,000 and manufacturing inefficiencies incurred as a result of the Michigan plant consolidation. As a percentage of sales, material and labor collectively increased 1.3%, while overhead increased 0.6%.

For the nine-month period ended September 30, 2014, gross margin decreased to 27.2% from 28.6% in the same period of 2013. This decrease is primarily due to higher employee health care costs and other fringe benefits of approximately \$800,000 and manufacturing inefficiencies incurred as a result of the Michigan plant consolidation. As a percentage of sales, material and labor collectively increased 0.2%, while overhead increased 1.2%.

Selling, General and Administrative Expenses

Selling, general, and administrative expenses (SG&A) increased approximately 3.4% to \$5.9 million for the three-month period ended September 30, 2014, from \$5.7 million for the same period in 2013. For the nine-month period ended September 30, 2014, SG&A increased approximately 2.6% to \$18.2 million from \$17.7 million in the same period in 2013. The increase in SG&A for the three-month period ended September 30, 2014, is primarily due to higher depreciation costs of approximately \$54,000 largely associated with the Company's new Enterprise Resource Planning (ERP) software system, increased bad debt expense of approximately \$102,000, and an increase of approximately \$75,000 in professional fees. The increase for the nine-month period ended September 30, 2014, is primarily due to higher depreciation costs of approximately \$151,000 largely associated with the Company's new ERP software system, increased employee health care costs of approximately \$175,000, and increased director compensation of approximately \$104,000.

Restructuring Costs

On January 7, 2014, the Company committed to move forward with a plan to cease operations at its Glendale Heights, Illinois plant and consolidate operations into its Grand Rapids, Michigan, facility. The Company's decision was in response to a pending significant increase in lease cost, declining sales at the Illinois facility, and significant anticipated savings as a result of the consolidation. The Company expects annual cost savings of approximately

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\$750,000 as a result of the Michigan plant consolidation. The consolidation into the Michigan facility is substantially complete and the actual costs incurred through September 30, 2014 are included in the table below.

On July 16, 2014, the Company committed to move forward with a plan to cease operations at its Costa Mesa, California, plant and consolidate operations into its Rancho Dominguez, California, facility and other UFP facilities. The Company's decision was in response to the upcoming December 31, 2014, expiration of the lease on the Costa Mesa facility as well as the close proximity of the two properties. The Company expects the activities related to this consolidation to be completed on or before December 31, 2014.

The Company expects to incur approximately \$535,000 in one-time expenses in connection with the consolidation of the California plants. Included in the \$535,000 amount are approximately \$50,000 of expenses the Company expects to incur relating to employee severance payments, approximately \$465,000 in moving expenses and expenses associated with vacating the Costa Mesa property and approximately \$20,000 in expenses in moving equipment within the Rancho Dominguez location. The Company does not expect to incur any lease separation costs as the completion of the move is expected to coincide with the expiration of the Costa Mesa lease. Total cash charges are estimated at \$535,000 and the actual costs incurred through September 30, 2014 are included in the table below. The Company expects annual cost savings of approximately \$550,000 as a result of the California plant consolidation.

The Company has recorded the following restructuring costs associated with the plant consolidations discussed above for the three and nine-month periods ended September 30, 2014 (in thousands):

| Restructuring Costs | Three Months Ended September 30, 2014 | | | Nine Months Ended September 30, 2014 | | |
|-----------------------------|--|------------|--------|---|------------|----------|
| | Michigan | California | Total | Michigan | California | Total |
| Employee severance payments | \$ 212 | \$ | \$ 212 | \$ 237 | \$ | \$ 237 |
| Relocation costs | 241 | 62 | 303 | 356 | 62 | 418 |
| Workforce training costs | 249 | | 249 | 362 | | 362 |
| Plant infrastructure costs | 8 | | 8 | 79 | | 79 |
| Total restructuring costs | \$ 710 | \$ 62 | \$ 772 | \$ 1,034 | \$ 62 | \$ 1,096 |

The Company also incurred approximately \$219,000 and \$350,000 for the three- and nine-month periods ended September 30, 2014, respectively, in related capital improvements at its Michigan facility.

Interest Expense

The Company had net interest expense of approximately \$20,000 and \$69,000 for the three- and nine-month periods ended September 30, 2014, respectively, compared to net interest expense of approximately \$43,000 and \$128,000, respectively, in the same periods of 2013. The decrease in interest expense in both periods is primarily due to a lower average debt balance as a result of the Company's repayment of term loans in conjunction with the execution of a new revolving credit facility in the fourth quarter of 2013.

Income Taxes

The Company's effective tax rate was approximately 35.0% for the three-month periods ended September 30, 2014, and 2013, respectively. The Company's effective tax rate was approximately 35.0% and 33.9%, respectively, for the nine-month periods ended September 30, 2014, and 2013. The increase in the effective tax rate in the nine-month period ended September 30, 2014, was a result of a retroactive application for a 2012 research and development credit which was recorded as a discrete event in the first quarter of 2013. Excluding this discrete event, the effective tax rate for the nine months ended September 30, 2013, was also approximately 35.0%.

Liquidity and Capital Resources

The Company generally funds its operating expenses, capital requirements, and growth plan through internally generated cash and bank credit facilities.

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Cash Flows

Net cash provided by operations for the nine-month period ended September 30, 2014, was approximately \$6.9 million and was primarily a result of net income generated of approximately \$6.0 million, an increase in refundable income taxes of approximately \$1.6 million, and an increase in accounts payable of approximately \$2.2 million due to the timing of vendor payments in the ordinary course of business. These cash inflows were partially offset by an increase in accounts receivable of approximately \$1.5 million due to strong September sales, an increase in inventory of approximately \$2.5 million due to the timing of raw materials purchases and customer shipments and a decrease in accrued expenses of approximately \$1.3 million due to payments for 2013 year-end bonuses, annual profit sharing contributions, and sales commissions.

Net cash used in investing activities during the nine-month period ended September 30, 2014, was approximately \$10.9 million and was primarily the result of additions of manufacturing machinery and equipment and the purchase of a new manufacturing facility in Texas.

Net cash used in financing activities was approximately \$251,000 in the nine-month period ended September 30, 2014, representing cash used to service term debt of approximately \$731,000 and to pay statutory withholding for stock options exercised and restricted stock units vested of approximately \$701,000, partially offset by excess tax benefits on share-based compensation of approximately \$845,000, and net proceeds received upon stock option exercises of approximately \$336,000.

Outstanding and Available Debt

The Company maintains an unsecured \$40 million revolving credit facility with Bank of America, N.A. The credit facility calls for interest of LIBOR plus a margin that ranges from 1.0% to 1.5% or, at the discretion of the Company, the bank's prime rate less a margin that ranges from 0.25% to zero. In both cases the applicable margin is dependent upon Company performance. Under the credit facility, the Company is subject to a minimum fixed-charge coverage financial covenant as well as a maximum total funded debt to EBITDA financial covenant. The Company's \$40 million credit facility matures on November 30, 2018.

As of September 30, 2014, the Company had no borrowings outstanding under the credit facility and the Company was in compliance with all covenants under the credit facility.

In 2012, the Company financed the purchase of two molded fiber machines through five-year term loans that mature in September 2017. The annual interest rate is fixed at 1.83% and the loans are secured by the related molded fiber machines. As of September 30, 2014, the outstanding balance of the term loan facility was approximately \$3.1 million.

Future Liquidity

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The Company requires cash to pay its operating expenses, purchase capital equipment, and to service its contractual obligations. The Company's principal sources of funds are its operations and its revolving credit facility. The Company generated cash of approximately \$6.9 million in operations during the nine-month period ended September 30, 2014, and cannot guarantee that its operations will generate cash in future periods. The Company's longer-term liquidity is contingent upon future operating performance.

Throughout fiscal 2014, the Company plans to continue to add capacity to enhance operating efficiencies in its manufacturing plants. The Company may consider additional acquisitions of companies, technologies, or products that are complementary to its business. The Company believes that its existing resources, including its revolving credit facility, together with cash expected to be generated from operations and funds expected to be available to it through any necessary equipment financings and additional bank borrowings, will be sufficient to fund its cash flow requirements, including capital asset acquisitions, through the next twelve months.

Commitments and Contractual Obligations

There have been no material changes outside the ordinary course of business to our contractual obligations and commitments, as disclosed in our Annual Report on Form 10-K for the year ended December 31, 2013.

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Off-Balance-Sheet Arrangements

The Company had no off-balance-sheet arrangements during the nine-month period ended September 30, 2014, other than operating leases.

ITEM 3: QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

There have been no material changes in our market risks as previously disclosed in Item 7A of our Annual Report on Form 10-K for the year ended December 31, 2013.

ITEM 4: CONTROLS AND PROCEDURES

As of the end of the period covered by this report (the Evaluation Date), the Company's management, under the supervision and with the participation of the Company's Chief Executive Officer and Chief Financial Officer, performed an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures (as defined in SEC Rule 13a-15(e) or 15d-15(e)). Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer concluded that, as of the Evaluation Date, the Company's disclosure controls and procedures were effective to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Securities Exchange Act of 1934, as amended, is (i) recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and (ii) accumulated and communicated to the Company's management, including the Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

There has been no change in the Company's internal control over financial reporting during the most recent fiscal quarter that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II: OTHER INFORMATION

ITEM 1A: RISK FACTORS

There have been no material changes from the risk factors previously disclosed in Part 1 - Item 1A of the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2013.

ITEM 6: EXHIBITS

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| Exhibit No. | Description |
|--------------------|---|
| 31.1 | Rule 13a-14(a)/15d-14(a) Certification of the Chief Executive Officer.* |
| 31.2 | Rule 13a-14(a)/15d-14(a) Certification of the Chief Financial Officer.* |
| 32.1 | Certifications pursuant to 18 U.S.C., Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.** |
| 101.INS | XBRL Instance Document.* |
| 101.SCH | XBRL Taxonomy Extension Schema Document.* |
| 101.CAL | XBRL Taxonomy Calculation Linkbase Document.* |
| 101.LAB | XBRL Taxonomy Label Linkbase Document.* |
| 101.PRE | XBRL Taxonomy Presentation Linkbase Document.* |
| 101.DEF | XBRL Taxonomy Extension Definition Linkbase Document.* |

* Filed herewith.

** Furnished herewith.

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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 thereunto duly authorized.

UFP TECHNOLOGIES, INC.

Date: November 7, 2014

By: /s/ R. Jeffrey Bailly
R. Jeffrey Bailly
Chairman, Chief Executive Officer,
President, and Director
(Principal Executive Officer)

Date: November 7, 2014

By: /s/ Ronald J. Lataille
Ronald J. Lataille
Chief Financial Officer
(Principal Financial Officer)

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