MICROPAC INDUSTRIES INC
Form 10QSB
October 10, 2006

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10 QSB

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

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

for the Quarter Ended August 26, 2006

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

MICROPAC INDUSTRIES, INC.

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

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act of 1934 during the past 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes X   No ____

On August 26, 2006, 2,578,315 shares of Common Stock, $.10 par value were outstanding.

MICROPAC INDUSTRIES, INC.

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PART I - FINANCIAL INFORMATION

ITEM 1 - FINANCIAL STATEMENTS

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

	For three months ended 08/26/06	08/27/05	Year-to-date 08/26/06	08
NET SALES	$ 4,552	$ 4,828	$ 13,085	$
COST AND EXPENSES:				
Cost of goods sold	(3,056)	(3,063)	(8,686)	
Research and development	(148)	(101)	(378)	
Selling, general & administrative expenses	(760)	(768)	(2,290)	
Total cost and expenses	(3,964)	(3,932)	(11,354)	
OPERATING INCOME BEFORE INTEREST AND INCOME TAXES	588	896	1,731	
Interest income	38	20	108	
INCOME BEFORE TAXES	$ 626	$ 916	$ 1,839	$
Provision for taxes	(238)	(348)	(699)	
NET INCOME	$ 388	$ 568	$ 1,140	$
NET INCOME PER SHARE, BASIC AND DILUTED	$ 0.15	$ 0.22	$ 0.44	$
DIVIDENDS PER SHARE	$ 0.00	$ 0.00	$ 0.15	$
WEIGHTED AVERAGE OF SHARES, Basic and diluted	2,578,315	2,578,315	2,578,315	2

See accompanying notes to financial statements.

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

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

ASSETS

CURRENT ASSETS	(Unaudited) 8/26/06	11/30/05
Cash and cash equivalents	$ 1,077	$ 1,722
Short term investments	2,936	2,527
Receivables, net of allowance for doubtful accounts of $89 on August 26, 2006 and November 30, 2005	2,541	3,057
Inventories:		
Raw materials	2,247	1,825
Work-in process	2,111	1,718
Total inventories	4,358	3,543
Prepaid expenses and other current assets	109	76
Deferred income tax	614	614
Total current assets	11,635	11,539
PROPERTY, PLANT AND EQUIPMENT, at cost:		
Land	80	80
Buildings	498	498
Facility improvements	796	796
Machinery and equipment	5,893	5,689
Furniture and fixtures	488	487
Total property, plant, and equipment	7,755	7,550
Less accumulated depreciation	(6,530)	(6,338)
Net property, plant, and equipment	1,225	1,212
Total assets	$ 12,860	$ 12,751

LIABILITIES AND SHAREHOLDERS' EQUITY

CURRENT LIABILITIES:		
Accounts payable	$ 550	$ 768
Accrued compensation	429	690
Other accrued liabilities	199	151
Deferred revenue	356	499
Income taxes payable	77	147

Total current liabilities	1,611	2,255
DEFERRED INCOME TAXES	74	74
SHAREHOLDERS' EQUITY		
Common stock, ($.10 par value), authorized 10,000,000 shares, 3,078,315 issued 2,578,315 outstanding at August 26, 2006 and November 30, 2005	308	308
Paid-in capital	885	885
Treasury stock, 500,000 shares, at cost	(1,250)	(1,250)
Retained earnings	11,232	10,479
Total shareholders' equity	11,175	10,422
Total liabilities and shareholders' equity	$ 12,860	$ 12,751

See accompanying notes to financial statements.

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

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

	Nine months ended 08/26/06	08/27/05
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 1,140	$ 1,695
Adjustments to reconcile net income to cash from operating activities:		
Depreciation and amortization	192	181
Changes in current assets and liabilities:		
Decrease (increase) in accounts receivable	516	(380)
Increase in inventories	(815)	(680)
Increase in prepaid expenses and other current assets	(33)	(20)
Decrease in income taxes, payable and deferred	(70)	(221)
(Decrease) increase in accounts payable	(218)	138
Decrease in accrued compensation	(261)	(114)
(Decrease) increase in other accrued liabilities and deferred revenues	(95)	96
Net cash provided by operating activities	356	695

CASH FLOWS FROM INVESTING ACTIVITIES:

Increase in short term investments	(409)	(125)
Additions to property, plant and equipment	(205)	(457)
Net cash used in investing activities	(614)	(582)
CASH FLOWS FROM FINANCING ACTIVITIES		
Cash dividend	(387)	(310)
Net cash used in financing activities	(387)	(310)
Net change in cash and cash equivalents	(645)	(197)
Cash and cash equivalents at beginning of period	1,722	1,239
Cash and cash equivalents at end of period	$ 1,077	$ 1,042
Supplemental Cash Flow Disclosure:		
Cash paid for income taxes	$ 815	$ 1,260

See accompanying notes to financial statements.

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

MICROPAC INDUSTRIES, INC.
NOTES TO FINANCIAL STATEMENTS
(Unaudited)

Note 1

In the opinion of management, the unaudited consolidated financial statements include all adjustments (consisting of only normal, recurring adjustments) necessary to present fairly the financial position as of August 26, 2006, the cash flows for the nine months ended August 26, 2006 and August 27, 2005, and the results of operations for the three months and nine months ended August 26, 2006 and August 27, 2005. Unaudited financial statements are prepared on a basis substantially consistent with those audited for the year ended November 30, 2005. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles in the United States have been condensed or omitted pursuant to the rules and regulations promulgated by the Securities and Exchange Commission. However, management believes that the disclosures contained are adequate to make the information presented not misleading.

Note 2

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

Note 3

On December 22, 2005, the Board of Directors of Micropac Industries, Inc. approved the payment of a $.15 per share dividend to all shareholders of record on February 3, 2006. The dividend was paid to shareholders on February 10, 2006.

On December 29, 2004, the Board of Directors of Micropac Industries, Inc. approved the payment of a $.12 per share dividend to all shareholders of record on January 25, 2005. The dividend was paid to shareholders on February 8, 2005.

Note 4

On March 1, 2001, the Company's shareholders approved the 2001 Employee Stock Option Plan (the "Stock Plan"). As of August 26, 2006 there were 500,000 options available to be granted. No options have been granted to date.

Note 5

On June 1, 2006 the Company renewed an uncollateralized $3,000,000 line of credit agreement with a bank. The interest rate is equal to the prime rate less 1/4%. The line of credit requires that the Company maintain certain financial ratios. The financial covenants require the Company to maintain a quick ratio of at least 1:1, maintain tangible net worth of $6,250,000 plus 75% of future net income, and maintain total liabilities to tangible net worth of less than 1.25:1. The Company is in compliance with these covenants. The Company has not, to date, used any of the available line of credit.

Note 6

Basic and diluted earnings per share are computed based upon the weighted average number of shares outstanding during the year. Diluted earnings per share gives effect to all dilutive potential common shares. For the three months and nine months ended August 26, 2006 and August 27, 2005, the Company had no dilutive potential common stock.

Note 7

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

MICROPAC INDUSTRIES, INC.
(Unaudited)

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

Business

Micropac Industries, Inc. (the "Company"), a Delaware corporation, manufactures and distributes various types of hybrid microelectronic circuits, solid state relays, power operational amplifiers, and optoelectronic components and assemblies. The Company's products are used as components in a broad range of military, space and industrial systems, including aircraft instrumentation and navigation systems, power supplies, electronic controls, computers, medical devices, and high-temperature (200o C) products. The Company's products are either custom (being application specific circuits designed and manufactured to meet the particular requirements of a single customer) or standard, proprietary components such as catalog items.

Results of Operations

	Three months ended		Year to Date	
	8/26/2006	8/27/2005	8/26/2006	8/27/2005
NET SALES	100.00%	100.00%	100.00%	100.00%
COST AND EXPENSES:				
Cost of Goods Sold	67.10%	63.50%	66.40%	60.90%
Research and development	3.30%	2.10%	2.90%	2.80%
Selling, general & administrative expenses	16.70%	15.90%	17.50%	16.90%
Total cost and expenses	87.10%	81.50%	86.80%	80.60%
OPERATING INCOME BEFORE INTEREST AND INCOME TAXES	12.90%	18.50%	13.20%	19.40%
Interest income	0.80%	0.50%	0.80%	0.40%
INCOME BEFORE TAXES	13.70%	19.00%	14.00%	19.80%
Provision for taxes	5.20%	7.20%	5.30%	7.50%
NET INCOME	8.50%	11.80%	8.70%	12.30%

Sales for the third quarter and nine months ended August 26, 2006 totaled $4,552,000 and $13,085,000, respectively. Sales for the third quarter decreased 5.7% or $276,000 below sales for the same period of 2005, while sales for the first nine months of 2006 decreased 5.4% or $746,000 below the first nine months of 2005. Sales decreased 51% in the commercial market, increased 1% in the military market, and increased 27% in the space market for the nine months ending August 26, 2006. The decrease in sales is primarily attributable to decreased sales to one major semiconductor customer on custom optoelectronic assemblies, offset by a increase in sale of standard products to distributors and an increase in the industrial product line.

Cost of goods sold for the third quarter 2006 versus 2005 totaled 67.10% and 63.50% of net sales, respectively, while cost of goods sold for the nine months of the comparable period totaled 66.40% and 60.90%, respectively. The cost of goods sold increase as a percentage of net sales of 5.50% is attributable to lower sales volume, changes in product mix, combined with stable fixed cost. As a percent of sales, overhead cost increased 5.3%, while labor and material cost were stable.

Selling, general and administrative expenses for the third quarter and first nine months of 2006 totaled 16.70% and 17.50% of net sales, respectively, compared to 15.90% and 16.90% for the same period in 2005. In actual dollars expensed, selling, general and administrative expenses decreased $8,000 in the third quarter of 2006, compared to 2005, and decreased $50,000 for the first nine months of 2006, versus 2005.

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Net income for the third quarter and year to date 2006 totaled $388,000 and $1,140,000, respectively, compared to $568,000 and $1,695,000 for the comparable periods in 2005. Net income per share totaled $.44 and $.66 for the comparable nine months of 2006 and 2005, respectively. The decrease in net income is associated with decreased sales to one major semiconductor customer on custom optoelectronic assemblies.

Total assets increased $109,000 to $12,860,000 as of August 26, 2006 from $12,751,000 as of November 30, 2005 with a decrease in cash and short-term investments of $236,000, raw material increase of $422,000, work in process increase of $393,000, accounts receivable decrease of $516,000, increase in prepaid expense of $33,000, and an increase in net property, plant, and equipment of $13,000.

Accounts receivable, net totaled $2,541,000 as of August 26, 2006 and represents a decrease of $516,000 since November 30, 2005, due to lower sales.

Inventories totaled $4,358,000 at the end of the third quarter 2006 compared to $3,543,000 on November 30, 2005, an increase of $815,000. Raw materials inventories increased $422,000 since November 30, 2005, while work-in-process inventories increased $393,000. The increase in raw materials and work-in-process is attributable to the purchase and receipt of long lead-time space level material. The value of these radiation tolerant parts is $561,000 in raw materials and $245,000 in work in process with a backlog value of $2,306,000.

Liabilities totaled $1,685,000 on August 26, 2006 representing a decrease of $644,000 from November 30, 2005; primarily associated with an decrease in accounts payable of $218,000, a decrease of $261,000 in accrued compensation, a reduction of $70,000 in provision for income taxes, a decrease in deferred revenue of $143,000, and a increase of $48,000 in other accrued liabilities.

Shareholders' equity increased $753,000 in the first nine months of 2006. Earnings per share for the nine month period totaled $.44 per share.

Liquidity and Capital Resources

Cash and short-term investments as of August 26, 2006 totaled $4,013,000 compared to $4,249,000 on November 30, 2005, a decrease of $236,000. Cash flow from operations was $356,000 for the first nine months offset by a cash dividend of $387,000 and $205,000 invested in automated production and test equipment.

For the nine months ended August 26, 2006 cash flows from operating activities were $356,000 compared to $695,000 for the nine months ended August 27, 2005.

Capital expenditures through the third quarter of 2006 totaled $205,000 compared to $457,000 as of August 27, 2005. These purchases were financed internally with the Company's cash, and included production and test equipment.

A special cash dividend of $387,000 was paid on February 3, 2006 to all shareholders of record.

On June 1, 2006 the Company renewed an uncollateralized $3,000,000 line of credit agreement with a bank. The interest rate is equal to the prime rate less 1/4%. The line of credit requires that the Company maintain certain financial ratios. The financial covenants require the Company to maintain a quick ratio of at least 1:1, maintain a tangible net worth of $6,250,000 plus 75% of future net income, and maintain a total liabilities to tangible net worth of less than 1.25:1. The Company is in compliance with these covenants. The Company has not, to date, used any of the available line of credit.

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

Outlook

New orders for the third quarter and year-to-date 2006 totaled $3,677,000 and $12,040,000, respectively, compared to $5,527,000 and $14,676,000 for the comparable periods of 2005 or a decrease of 33.5% and 18.0% respectively. The decrease in new orders is primarily attributable to the $1,826,000 decreased orders from one major semiconductor customer on custom optoelectronic assemblies.

Backlog totaled $8,295,000 on August 26, 2006 compared to $10,044,000 as of August 27, 2005 and $9,319,000 on November 30, 2005. The majority of the backlog is expected to be shipped in the next twelve (12) months and represents a good mix of the company's products and technologies with 12% in the commercial market, 54% in the military market, and 34% in the space market compared to 11% in the commercial market, 57% in the military market, and 32% in the space market for the same period of 2005.

The Company cannot assure that the results of operations for the interim period presented are indicative of total results for the entire year due to fluctuations in customer delivery schedules, or other factors over which the Company has no control.

Cautionary Statement

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

Such risks and uncertainties include, but are not limited to historical volatility and cyclicality of the semiconductor and semiconductor capital equipment markets that are subject to significant and often rapid increases and decreases in demand. In addition, the Company produces silicon phototransistors and light emitting diode die for use in certain military, standard and custom products. Fabrication efforts sometimes may not result in successful results, limiting the availability of these components. Competitors offer commercial level alternatives and our customers may purchase our competitors' products if the Company is not able to manufacture the products using these technologies to meet the customer demands. Approximately $1,278,000 of the Company's backlog is dependent on these semiconductors.

The Company disclaims any responsibility to update the forward-looking statements contained herein, except as may be required by law.

ITEM 3. CONTROLS AND PROCEDURES

(a) Evaluation of disclosure controls and procedures.

The Chief Executive Officer and Chief Financial Officer of the Company evaluated the Company's disclosure controls and procedures (as defined in Exchange Act Rules 13a-15 (e) as of August 26, 2006 and, based on this evaluation, concluded that the Company's disclosure controls and procedures are functioning in an effective manner to ensure that the information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act, is recorded, processed, summarized and reported, within the time periods specified in the SEC's rules and forms. .

(b) Changes in internal controls.

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

PART II - OTHER INFORMATION

ITEM 1. LEGAL PROCEEDINGS

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

ITEM 2. CHANGES IN SECURITIES

None

ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None

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

None

ITEM 5. OTHER INFORMATION

None

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K

(a) Exhibits

31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes- Oxley Act of 2002
31.2 Certification of Chief Accounting Officer pursuant to Section 302 of the Sarbanes- Oxley Act of 2002
32.1 Certification of Chief Executive Officer pursuant to 18 U.S.C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley act of 2002.
32.2 Certification of Chief Accounting Officer pursuant to U. S. C. section 1350, as adopted pursuant to section 906 of the Sarbanes-Oxley act of 2002.

(b) Reports on Form 8-K

On December 22, 2005, the Board of Directors of Micropac Industries, Inc. approved the payment of a $.15 per share dividend to all shareholders of record on February 3, 2006. The dividend was paid to shareholders on February 10, 2006

SIGNATURES

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

MICROPAC INDUSTRIES, INC.

October 06, 2006	/s/ Mark King
Date	Mark King Chief Executive Officer
October 06, 2006	/s/ Patrick Cefalu
Date	Patrick Cefalu Chief Financial Officer