

United States
SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-Q

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

For quarterly period ended June 30, 1994

Commission File Number 0-2382

MTS SYSTEMS CORPORATION
(Exact name of registrant as specified in its charter)

MINNESOTA
(State or other jurisdiction of
incorporation or organization)

612-937-4000
(Telephone number of registrant
including area code)

41-0908057
(I.R.S. Employer
Identification No.)

14000 Technology Drive, Eden Prairie, Minnesota 55344
(Address/Zip Code of 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 the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common Stock, \$.25 par value; 4,605,678 shares outstanding.

PART I. FINANCIAL INFORMATION

MTS SYSTEMS CORPORATION AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
JUNE 30, 1994 AND SEPTEMBER 30, 1993

ASSETS	JUNE	SEPT 30
	1994	1993
	UNAUDITED	AUDITED

	(expressed in \$ 000's)	
Cash and cash equivalents	\$8,195	\$7,597
Accounts receivable	45,569	41,841
Unbilled contracts and retainage receivable	30,754	47,066
Inventories-		

Customer jobs-in-process	11,542	7,394
Components, assemblies and parts	20,588	17,615
Prepaid expenses	5,355	1,932
	-----	-----
Total current assets	122,003	123,445
	-----	-----
Land	3,703	3,725
Buildings and improvements	36,127	27,532
Machinery and equipment	49,367	45,376
Accumulated depreciation	(42,074)	(39,379)
	-----	-----
Total property and equipment	47,123	37,254
	-----	-----
Other assets	5,770	5,017
	-----	-----
	\$174,896	\$165,716
	=====	=====
LIABILITIES AND SHAREHOLDERS' INVESTMENT		
Notes payable to banks	\$23,317	\$28,602
Current maturities of long-term debt	1,037	2,194
Accounts payable	10,455	6,882
Accrued compensation and benefits	15,416	16,085
Accrued income taxes	1,592	726
Other accrued liabilities	8,011	5,148
Advance billings to customers	6,514	7,324
	-----	-----
Total current liabilities	66,342	66,961
	-----	-----
Deferred income taxes	2,651	3,241
Long-term debt, less current maturities	6,638	2,503
	-----	-----
Common stock, \$.25 par; 16,000,000 shares authorized: 4,605,678 and 4,543,603 shares issued and outstanding	1,151	1,136
Additional paid-in capital	3,801	2,677
Retained earnings	90,281	85,661
Cumulative translation adjustment	4,032	3,537
	-----	-----
Total shareholders' investment	99,265	93,011
	-----	-----
	\$174,896	\$165,716
	=====	=====

MTS SYSTEMS CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
FOR THE THREE MONTHS ENDED JUNE 30, 1994 AND 1993
(UNAUDITED)

	FOR THE 3 MONTHS ENDED JUNE 30	
	1994	1993

	(expressed in 000's except for per share amounts)	
NET SALES	\$48,468	\$48,824
COST OF SALES	29,566	28,698
	-----	-----
Gross profit	18,902	20,126
OPERATING EXPENSES:		
Selling	10,744	9,668
General and administrative	3,406	2,790
Research and development	3,253	2,769
Interest expense	552	567
Interest income	(116)	(109)
Other (income) and expense, net (including \$.7 million gain from real estate transaction in 1993)	(379)	80
	-----	-----
Total operating expense	17,460	15,765
	-----	-----
INCOME BEFORE INCOME TAXES	1,442	4,361
PROVISION FOR INCOME TAXES	440	1,497

NET INCOME	\$1,002	\$2,864
	=====	=====
EARNINGS PER COMMON AND COMMON EQUIVALENT SHARE	\$0.21	\$0.63
	=====	=====
DIVIDENDS PER SHARE	\$0.14	\$0.12
	=====	=====
BACKLOG	\$89,327	\$99,405
	=====	=====
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING	4,686	4,580
	=====	=====

MTS SYSTEMS CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
FOR THE NINE MONTHS ENDED JUNE 30, 1994 AND 1993
(UNAUDITED)

	FOR THE 9 MONTHS ENDED JUNE 30	
	1994	1993

	(expressed in 000's except for per share amounts)	
NET SALES	\$142,065	\$132,008
COST OF SALES	86,340	77,306
	-----	-----
Gross profit	55,725	54,702
OPERATING EXPENSES:		
Selling	29,667	27,017
General and administrative	9,429	7,719
Research and development	9,282	8,694
Interest expense	1,504	1,316
Interest income	(211)	(379)
Other (income) and expense, net (including \$3.7 and \$.7 million gain from real estate transactions in 1994 and 1993, respectively	(3,929)	138
	-----	-----
Total operating expense	45,742	44,505
	-----	-----
INCOME BEFORE INCOME TAXES	9,983	10,197
PROVISION FOR INCOME TAXES	3,440	3,471
	-----	-----
NET INCOME	\$6,543	\$6,726
	=====	=====
EARNINGS PER COMMON AND COMMON EQUIVALENT SHARE	\$1.40	\$1.48
	=====	=====
DIVIDENDS PER SHARE	\$0.42	\$0.36
	=====	=====
BACKLOG	\$86,327	\$99,405
	=====	=====
WEIGHTED AVERAGE COMMON SHARES OUTSTANDING	4,679	4,546
	=====	=====

MTS SYSTEMS CORPORATION AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE NINE MONTHS ENDED JUNE 30, 1994 AND 1993
(UNAUDITED)

	FOR THE 9 MONTHS ENDED	
	JUN 30	JUN 30
	1994	1993
	(expressed in \$000's)	
OPERATING ACTIVITIES		
Net income	\$6,543	\$6,726
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation and amortization	4,492	4,068
Deferred income taxes	(590)	(100)
Foreign currency translation adjustment	495	(954)
Changes in operating assets and liabilities:		
Receivables, including accounts, unbilled contracts and retainages	12,584	(9,777)
Inventories	(7,121)	(5,716)
Prepaid expenses	(3,423)	(1,007)
Accrued income taxes	867	(1,210)
Advance billings to customers	(811)	348
Other, net	5,767	3,389
NET CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES	18,803	(4,233)
INVESTING ACTIVITIES		
Property and equipment, net	(14,108)	(3,246)
Investment in Custom Servo Motors, Inc.	--	(471)
Excess purchase cost over assets acquired in Adamel Lhomargy	(40)	--
Other assets	(967)	541
NET CASH USED IN INVESTING ACTIVITIES	(15,115)	(3,176)
FINANCING ACTIVITIES		
Net borrowings (payments) on notes payable	(5,285)	12,439
Proceeds from issuance of long-term debt	9,690	--
Payments on long-term borrowings	(6,711)	(2,238)
Cash dividends	(1,923)	(1,606)
Proceeds from employee stock option and stock purchase plans	1,165	1,033
Payments to purchase and retire common stock	(26)	(1,177)
NET CASH PROVIDED BY FINANCING ACTIVITIES	(3,090)	8,451
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	598	1,042
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	7,597	9,277
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$8,195	\$10,319

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

CONSOLIDATION AND TRANSLATION. The consolidated financial statements include the accounts of MTS SYSTEMS CORPORATION (the Company) and its wholly owned subsidiaries. All significant intercompany balances and transactions have been eliminated.

All balance sheet accounts of foreign subsidiaries are translated at the current exchange rate as of the end of the accounting period. Income statement items are translated at average currency exchange rates. The resulting

translation adjustment is recorded as a separate component of shareholders' investment. Gains and losses resulting from foreign currency transactions are included in "Other (income) and expense, net" in the consolidated Statements of Income.

REVENUE RECOGNITION. Revenue is recognized upon shipment of equipment when the customer's order can be manufactured and delivered in less than nine months. Revenue on contracts requiring longer delivery periods (long-term contracts) and other customized orders which permit progress billings is recognized using the percentage of completion method based on the cost incurred to date relative to estimated total cost of the contract (cost-to-cost method). The cumulative effects of revisions of estimated total contract costs and revenues are recorded in the period in which the facts become known. When a loss is anticipated on a contract, the amount thereof is provided currently.

LONG-TERM CONTRACTS. The Company enters into long-term contracts for customized equipment sold to its customers. Under terms of certain contracts, revenue recognized using the percent of completion method may not be invoiced until completion of contractual milestones, upon shipment of the equipment, or upon installation and acceptance by the customer. Unbilled amounts for such contracts appear in the consolidated balance sheets as unbilled contracts and retainage receivable. Amounts unbilled or retained at June 30, 1994 are expected to be invoiced as follows: \$22,322,000 in 1994 and \$8,432,000 in 1995.

INCOME TAXES -- CHANGE IN ACCOUNTING METHOD. Effective October 1, 1993, the Company adopted Statement of Financial Accounting Standards No. 109, Accounting for Income Taxes (SFAS No. 109), under which deferred income tax assets and liabilities are recognized for the differences between financial and income tax reporting bases of assets and liabilities based on enacted tax rates and laws. Provision for Income Taxes is the tax payable or refundable for the period plus or minus the change during the period in deferred tax assets and liabilities.

The cumulative effect of adopting SFAS No. 109 was not significant. The impact of the Company's change in accounting for income taxes on the results of operations for the quarters ended December 31, 1993 and June 30, 1994 was also not significant.

ACQUISITION. During the quarter ended March 31, 1994, the Company acquired the stock of Adamel-Lhomargy, a French manufacturer of material testing systems, for cash and assumption of debt. The Consolidated Balance Sheet at June 30, 1994 includes the assets and liabilities of Adamel, and the Consolidated Statement of Income for the three and nine months periods ended June 30, 1994 includes the operations of Adamel from the effective date of the acquisition.

Adamel had revenues of under \$10 million in its most recent fiscal year. Neither the balance sheet nor the results of operations for Adamel's most recent fiscal year or the quarter ended June 30, 1994 were significant with respect to the Company's Consolidated Balance Sheets or Consolidated Statements of Income prepared as of September 30, 1993 or June 30, 1994, respectively.

OTHER FINANCIAL STATEMENT DISCLOSURE. The Notes to Consolidated Financial Statements appearing in the Company's September 30, 1993 Annual Report to Shareholders on pages 22 through 28 are incorporated herein by reference.

MANAGEMENT'S INTERIM FINANCIAL STATEMENT REPRESENTATION. The unaudited interim financial statements furnished herein reflect all adjustments which are, in the opinion of management, necessary to a fair statement of the results of the interim periods presented.

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

New Orders and Backlog

New orders for the third quarter of fiscal 1994, ended June 30 were \$51,242,000, a 29% increase over the comparable quarter in fiscal 1993. Orders in the Mechanical Testing and Simulation sector increased 28% from the same quarter in 1993. Large dollar orders for the quarter were 23% of new orders in 1994 and 1993. Orders in the Measurement and Automation sector increased 38% for the quarter ended in 1994 compared to the same quarter in 1993.

New orders for the nine months ended June 30, 1994 were \$141,512,000 compared to \$131,970,000 for the same period one year ago, a 7% increase. Orders in the Mechanical Testing and Simulation sector were 2% higher than last year while orders in the Measurement and Automation sector were 38% ahead of last year. Large orders comprise 25% of the total in 1994 compared to 34% of the 1993 order volume. International orders were 52% of the 1994 total compared to 46% for 1993.

Backlog of undelivered orders at June 30, 1994 was \$89,327,000

compared to \$99,405,000 at March 31, 1993 and \$88,731,000 at September 30, 1993.

Results of Operations

Revenues for the third quarter were \$48,468,000, a 1% decrease from the same quarter one year ago. International content of revenue was 53% and 47% for the quarters ended June 30, 1994 and 1993, respectively.

Income before income taxes decreased 67% to \$1,442,000 compared to \$4,361,000 for the second quarter ended a year ago. The decrease in pretax earnings resulted from lower gross margins on 1994 projects and increased operating expenses. Certain large custom-content projects in the Company's Mechanical Testing and Simulation sector are experiencing lower gross margins arising from technical challenges and competitive pricing pressure. Operating expenses increased nearly \$1.7 million, principally in selling, administration and in product development. The increase reflects investments in domestic servo motor business and markets in the Far-east and Europe, including the new French acquisition. Such investments are consistent with revenue growth in those areas.

Net income for the quarter was \$1,002,000 a 65% decrease compared to the comparable quarter one year ago. The effective tax rate for the quarter ended June 30, 1994 was 30% compared to 34% for the quarter ended in June, 1993.

Revenues for the nine months ended in June, 1994 were \$142,065,000, an 8% increase from the \$132,008,000 reported one year ago. International revenues were 51% compared to 50% for the periods ended in June of 1994 and 1993, respectively. Revenues in the Material Testing and Simulation sector increased 3% while Measurement and Automation revenues increased 33% over revenues reported one year ago.

Income before income taxes for the first nine months of 1994, decreased 2% to \$9,983,000 from \$10,197,000 reported in 1993. Gross margins as a percent of sales were 39.2% in 1994 compared to 41.4% in 1993. The decline in margins is discussed above and is the principal reason for the decline in pretax income. The effect of reduced gross margin was offset by a \$3.7 million non-operating gain from the sale of the Berlin plant, reported in the second quarter. Operating expenses (exclusive of the gain in 1994 and a similar, though much smaller, gain in 1993) as a percent of sales were 34.8% compared to 34.2% for the nine months ended in June, 1994 and 1993, respectively.

Net income for the first nine months of 1994 was \$6,543,000 compared to \$6,726,000 reported one year ago, a 3% decrease. The income tax rates were 34% and 34% for the nine months ended in 1994 and 1993, respectively.

The cumulative effect of the Company's change in accounting to adopt SFAS No. 109 was not significant. The impact of the change on the results of operations for the quarters ended in December, 1993, March, 1994 and June also were not significant.

Financial Condition and Liquidity

The ratio of current assets to current liabilities was 1.8 at June 30, 1994 and September 30, 1993. Cash and cash equivalents were \$8,195,000 at June 30, 1994 compared to \$7,597,000 at September 30, 1993. The Company's borrowing under its \$70 million lines of credit was \$23 million at June 30, 1994 compared to \$29 million at September 30, 1993.

Capital expenditures, net of retirements for the nine months totalled \$14,108,000. The purchase of a new Berlin plant facility accounts for \$10 million of the expenditure. The Company's total debt to equity ratio decreased to 31% at June 30, 1994 from 36% at September 30, 1993. However, MTS undertook additional debt to purchase the new plant in Berlin and acquire Adamel-Lhomargy during the nine month period ended in June. The resulting decrease in the total debt to equity ratio reflects conversion of unbilled receivables to cash over the nine months and use of the proceeds from the sale of its old facility in Berlin to repay a portion of the additional financing undertaken. Negotiations are underway to restructure the remaining indebtedness with a mortgage.

The Company's past financial performance, the availability of credit under its borrowing facilities, available cash and cash equivalents provide sufficient resources for growth, expansion and diversification.

SIGNATURES

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

MTS SYSTEMS CORPORATION

/s/ D.M. Sullivan
D.M. Sullivan
Chairman, President and
Chief Executive Officer

/s/ M.L. Carpenter
M.L. Carpenter
Vice President
Chief Financial Officer

Dated: August 12, 1994