SYPRIS SOLUTIONS INC
Form 10-Q
August 08, 2007
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# UNITED STATES

# SECURITIES AND EXCHANGE COMMISSION

**Washington D.C. 20549**

# FORM 10-Q

**(Mark One)**

**x Quarterly Report Pursuant To Section 13 Or 15(d) Of The Securities Exchange Act Of 1934**
**For the quarterly period ended July 1, 2007**

**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: 0-24020**

# SYPRIS SOLUTIONS, INC.

**(Exact name of registrant as specified in its charter)**

| | |
|---|---|
| **Delaware**<br>**(State or other jurisdiction of**<br>**incorporation or organization)** | **61-1321992**<br>**(I.R.S. Employer**<br>**Identification No.)** |
| **101 Bullitt Lane, Suite 450** | **(502) 329-2000** |

| | |
|---|---|
| **Louisville, Kentucky 40222** | |
| **(Address of principal executive offices) (Zip code)** | **(Registrant s telephone number, including area code)** |

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. x Yes ¨ No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

¨ Large accelerated filer x Accelerated filer ¨ Non-accelerated filer

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

As of July 31, 2007, the Registrant had 19,142,022 shares of common stock outstanding.

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**PART I. FINANCIAL INFORMATION**

**ITEM 1. FINANCIAL STATEMENTS**

**SYPRIS SOLUTIONS, INC.**

**CONSOLIDATED STATEMENTS OF OPERATIONS**

**(in thousands, except for per share data)**

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | July 1, 2007 | June 30, 2006 | July 1, 2007 | June 30, 2006 |
| | (Unaudited) | | (Unaudited) | |
| Net revenue: | | | | |
| Outsourced services | $ 91,338 | $ 115,419 | $ 186,344 | $ 224,230 |
| Products | 24,909 | 16,814 | 41,342 | 37,998 |
| Total net revenue | 116,247 | 132,233 | 227,686 | 262,228 |
| Cost of sales: | | | | |
| Outsourced services | 87,156 | 109,688 | 173,405 | 210,831 |
| Products | 21,390 | 12,111 | 34,573 | 28,346 |
| Total cost of sales | 108,546 | 121,799 | 207,978 | 239,177 |
| Gross profit | 7,701 | 10,434 | 19,708 | 23,051 |
| Selling, general and administrative | 8,775 | 9,376 | 19,371 | 18,874 |
| Research and development | 714 | 371 | 1,393 | 704 |
| Amortization of intangible assets | 164 | 158 | 328 | 317 |
| Nonrecurring items | 1,248 | 256 | 1,554 | 677 |
| Operating (loss) income | (3,200) | 273 | (2,938) | 2,479 |
| Interest expense, net | 914 | 1,083 | 1,633 | 2,242 |
| Other expense (income), net | 61 | (8) | 41 | (258) |
| (Loss) income before income taxes | (4,175) | (802) | (4,612) | 495 |
| Income tax (benefit) expense | (1,874) | (358) | (2,066) | 83 |
| Net (loss) income | $ (2,301) | $ (444) | $ (2,546) | $ 412 |
| (Loss) earnings per common share: | | | | |
| Basic | $ (0.13) | $ (0.02) | $ (0.14) | $ 0.02 |
| Diluted | $ (0.13) | $ (0.02) | $ (0.14) | $ 0.02 |
| Dividends declared per common share | $ 0.03 | $ 0.03 | $ 0.06 | $ 0.06 |
| Weighted average shares outstanding: | | | | |
| Basic | 18,169 | 18,065 | 18,138 | 18,055 |
| Diluted | 18,169 | 18,065 | 18,138 | 18,237 |

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

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**SYPRIS SOLUTIONS, INC.**

**CONSOLIDATED BALANCE SHEETS**

**(in thousands, except for share data)**

| | July 1, 2007 (Unaudited) | December 31, 2006 (Note) |
|---|---|---|
| **ASSETS** | | |
| Current assets: | | |
| Cash and cash equivalents | $ 19,398 | $ 32,400 |
| Restricted cash | 883 | 1,002 |
| Accounts receivable, net | 60,974 | 59,876 |
| Inventory, net | 80,570 | 74,146 |
| Other current assets | 32,503 | 34,014 |
| Total current assets | 194,328 | 201,438 |
| Property, plant and equipment, net | 145,309 | 155,341 |
| Goodwill | 14,277 | 14,277 |
| Other assets | 8,344 | 7,977 |
| Total assets | $ 362,258 | $ 379,033 |
| **LIABILITIES AND STOCKHOLDERS EQUITY** | | |
| Current liabilities: | | |
| Accounts payable | $ 73,130 | $ 76,291 |
| Accrued liabilities | 20,468 | 19,430 |
| Current portion of long-term debt | | 5,000 |
| Total current liabilities | 93,598 | 100,721 |
| Long-term debt | 48,000 | 55,000 |
| Other liabilities | 13,286 | 13,426 |
| Total liabilities | 154,884 | 169,147 |
| Stockholders equity: | | |
| Preferred stock, par value $0.01 per share, 975,150 shares authorized; no shares issued | | |
| Series A preferred stock, par value $0.01 per share, 24,850 shares authorized; no shares issued | | |
| Common stock, non-voting, par value $0.01 per share, 10,000,000 shares authorized; no shares issued | | |
| Common stock, par value $0.01 per share, 30,000,000 shares authorized; 19,179,117 shares issued and 19,136,105 outstanding in 2007 and 18,342,243 shares issued and 18,338,484 outstanding in 2006 | 191 | 183 |
| Additional paid-in capital | 145,011 | 143,537 |
| Retained earnings | 66,130 | 69,816 |
| Accumulated other comprehensive loss | (3,762) | (3,634) |
| Treasury stock, 43,012 and 3,759 shares in 2007 and 2006, respectively | (196) | (16) |
| Total stockholders equity | 207,374 | 209,886 |
| Total liabilities and stockholders equity | $ 362,258 | $ 379,033 |

Note: The balance sheet at December 31, 2006 has been derived from the audited consolidated financial statements at that date but does not include all information and footnotes required by accounting principles generally accepted in the United States for a complete set of financial statements.

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

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**SYPRIS SOLUTIONS, INC.**

**CONSOLIDATED CASH FLOW STATEMENTS**

**(in thousands)**

| | Six Months Ended July 1, 2007 | Six Months Ended June 30, 2006 |
|---|---|---|
| | (Unaudited) | (Unaudited) |
| Cash flows from operating activities: | | |
| Net (loss) income | $ (2,546) | $ 412 |
| Adjustments to reconcile net (loss) income to net cash provided by operating activities: | | |
| Depreciation and amortization | 14,254 | 13,678 |
| Noncash compensation expense | 462 | 448 |
| Other noncash items | 27 | (1,520) |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | (831) | (1,814) |
| Inventory | (1,843) | 6,161 |
| Other current assets | (3,328) | (3,448) |
| Accounts payable | (3,258) | 15,827 |
| Accrued liabilities | 1,492 | (156) |
| Net cash provided by operating activities | 4,429 | 29,588 |
| Cash flows from investing activities: | | |
| Capital expenditures, net | (3,612) | (4,903) |
| Proceeds from sale of assets | 22 | 57 |
| Changes in nonoperating assets and liabilities | (891) | 431 |
| Net cash used in investing activities | (4,481) | (4,415) |
| Cash flows from financing activities: | | |
| Net change in debt under revolving credit agreements | 13,000 | (10,000) |
| Payments on Senior Notes | (25,000) | |
| Cash dividends paid | (1,117) | (1,094) |
| Proceeds from issuance of common stock | 167 | 209 |
| Net cash used in financing activities | (12,950) | (10,885) |
| Net (decrease) increase in cash and cash equivalents | (13,002) | 14,288 |
| Cash and cash equivalents at beginning of period | 32,400 | 12,060 |
| Cash and cash equivalents at end of period | $ 19,398 | $ 26,348 |

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

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**Sypris Solutions, Inc.**

**Notes to Consolidated Financial Statements**

**(1) Nature of Business**

Sypris is a diversified provider of outsourced services and specialty products. The Company performs a wide range of manufacturing, engineering, design, testing, and other technical services, typically under multi-year, sole-source contracts with corporations and government agencies in the markets for truck components & assemblies, aerospace & defense electronics, and test & measurement equipment.

**(2) Basis of Presentation**

The accompanying unaudited consolidated financial statements include the accounts of Sypris Solutions, Inc. and its wholly-owned subsidiaries (collectively, Sypris or the Company), and have been prepared by the Company in accordance with the rules and regulations of the Securities and Exchange Commission. All significant intercompany transactions and accounts have been eliminated. These unaudited consolidated financial statements reflect, in the opinion of management, all material adjustments (which include only normal recurring adjustments) necessary to fairly state the results of operations, financial position and cash flows for the periods presented, and the disclosures herein are adequate to make the information presented not misleading. Preparing financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses. Actual results for the three and six months ended July 1, 2007 are not necessarily indicative of the results that may be expected for the year ending December 31, 2007. These unaudited consolidated financial statements should be read in conjunction with the consolidated financial statements, and notes thereto, for the year ended December 31, 2006 as presented in the Company s Annual Report on Form 10-K.

Certain prior period amounts have been reclassified to conform to the current period presentation.

**(3) Recent Accounting Pronouncements**

In September 2006, the Financial Accounting Standards Board ( FASB ) issued Statement of Financial Accounting Standards ( SFAS ) No. 157, Fair Value Measurements . The objective of SFAS No. 157 is to increase consistency and comparability in fair value measurements and to expand disclosures about fair value measurements. SFAS No. 157 defines fair value, establishes a framework for measuring fair value in generally accepted accounting principles, and expands disclosures about fair value measurements. SFAS No. 157 applies under other accounting pronouncements that require or permit fair value measurements and does not require any new fair value measurements. The provisions of SFAS No. 157 are effective for fair value measurements made in fiscal years beginning after November 15, 2007. The adoption of this statement is not expected to have a material effect on the Company s future reported financial position or results of operations.

**(4) Major Customer Chapter 11 Filing**

On March 3, 2006 (Filing Date), the Company s largest customer, Dana Corporation (Dana), and 40 of its U.S. subsidiaries, filed voluntary petitions for reorganization under Chapter 11 of the U.S. Bankruptcy Code in the U.S. Bankruptcy Court for the Southern District of New York. Dana s European, South American, Asia-Pacific, Canadian and Mexican subsidiaries were excluded from the Chapter 11 filing. On May 10, 2006, the Company reached an agreement (Agreement) with Dana (Debtor-in-Possession) under which both parties agreed, among other things, that Dana (Debtor-in-Possession) owed the Company approximately $22,100,000, and that the Company owed Dana approximately $11.8 million or a difference of approximately $10.3 million subject to final reconciliation. Of this amount, the Agreement also provided the Company with a $9,200,000 progress payment on May 11, 2006, as well as reduced payment terms on a prospective basis. As of December 31, 2006, Dana and the Company had substantially completed the reconciliation process under the Agreement and the Company expected approximately $1,100,000 in net additional accounts receivable to be collected from Dana (Debtor in Possession), although Dana had not yet paid such amounts. The Company also had a $3,300,000 refundable deposit with Dana for a specified business line yet to be transferred to the Company.

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In addition, on December 6, 2006, an independent arbitrator initially held that Dana had breached certain of its agreements with Sypris by failing to transfer certain volumes of business and by failing to pay the appropriate prices for the volumes that were transferred. As a result, the arbitrator awarded payments to Sypris totaling $1,818,212 plus $146,258 per month on an ongoing basis. The arbitration ruling was subject to a 30-day clarification period and was not included in the 2006 consolidated balance sheet. On January 29, 2007, this award became final; and accordingly, net revenue in the consolidated statements of operations for the six months ended July 1, 2007 includes $2,695,760 pertaining to the arbitration award. See Note 14 for Dana related subsequent events.

**(5) Stock-Based Compensation**

On May 14, 2007 the Company offered eligible participants, including executive officers and directors of the Company, the opportunity to surrender certain vested outstanding, unexercised stock options which have exercise prices greater than $7.90 per share in exchange for shares of common stock or new options to acquire common stock with an exercise price of $7.90 per share, pursuant to the 2004 Sypris Equity Plan. Participants could participate in the offer if they remained employed through June 13, 2007, the date on which the Company canceled eligible options under the offer. At the participant s election, the participant could exchange all of the eligible options owned by such participant for either (i) shares of common stock having a fair value equivalent to the fair value of each such eligible option, or (ii) new options to purchase shares of Sypris common stock having a fair value equivalent to the fair value of each such eligible option.

The ratio of shares subject to eligible options cancelled to common stock and new options issued was calculated using the Black-Scholes Merton Option Valuation Model. If a participant elected to exchange any eligible options, he or she also surrendered any target performance options granted under any Sypris equity plan. Each share of common stock and new option granted with respect to an exchanged option was fully vested. All new options are exercisable through May 14, 2011 unless earlier forfeited.

The following table summarizes option activity for the six months ended July 1, 2007:

| | Number of Shares | Weighted-average Exercise Price Per Share | Weighted-average Remaining Term | Aggregate Intrinsic Value |
|---|---|---|---|---|
| Outstanding at January 1, 2007 | 2,303,317 | $ 10.08 | | |
| Granted | 382,529 | 7.88 | | |
| Exchanged | (1,101,655) | 11.93 | | |
| Forfeited | (58,640) | 9.44 | | |
| Expired | (105,000) | 7.44 | | |
| Exercised | (57,997) | 6.17 | | |
| Outstanding at July 1, 2007 | 1,362,554 | $ 8.37 | 3.52 | $ 615,985 |
| Exercisable at July 1, 2007 | 1,061,308 | $ 8.12 | 3.29 | $ 591,451 |

Pursuant to the Exchange Offer and in exchange for the options surrendered, the Company issued 159,974 shares of common stock, in addition to 374,529 options to purchase common stock. Additionally, participants surrendered 150,500 Target Options under the program, which represented all remaining Target Options outstanding at the date of exchange.

On January 12, 2007, the Company granted 258,000 restricted stock awards under a key employee retention program which vest over two or four years, as applicable. On March 1, 2007, the Company also granted 305,290 restricted stock awards under a long-term incentive program. Twenty-five percent of the restricted stock awards will vest in one-third increments on each of the third, fifth and seventh anniversaries of the grant date. Seventy-five percent of the restricted stock awards will vest in one-quarter increments on each of the first, second, third and fourth anniversaries of the achievement of the Vesting Trigger Date. This Vesting Trigger Date is the first business day following the Company s achievement of a specified target for aggregate net income as measured over the previous four fiscal quarters. If no Vesting Trigger Date occurs before March 1, 2010, this portion of the restricted stock awards will be immediately forfeited.

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**(6) (Loss) Earnings Per Common Share**

There were no adjustments required to be made to net (loss) income for purposes of computing basic and diluted (loss) earnings per common share. A reconciliation of the weighted average shares outstanding used in the calculation of basic and diluted (loss) earnings per common share is as follows (in thousands):

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | July 1, 2007 | June 30, 2006 | July 1, 2007 | June 30, 2006 |
| | (Unaudited) | | (Unaudited) | |
| Shares used to compute basic (loss) earnings per common share | 18,169 | 18,065 | 18,138 | 18,055 |
| Dilutive effect of equity awards | | | | 182 |
| Shares used to compute diluted (loss) earnings per common share | 18,169 | 18,065 | 18,138 | 18,237 |

**(7) Inventory**

Inventory consisted of the following (in thousands):

| | July 1, 2007 | December 31, 2006 |
|---|---|---|
| | (Unaudited) | |
| Raw materials, including perishable tooling of $1,546 and $1,276 in 2007 and 2006, respectively | $ 24,930 | $ 28,885 |
| Work in process | 12,193 | 12,576 |
| Finished goods | 8,796 | 10,129 |
| Costs relating to long-term contracts and programs, net of amounts attributed to revenue recognized to date | 45,134 | 40,451 |
| Progress payments related to long-term contracts and programs | (3,999) | (11,107) |
| Reserve for excess and obsolete inventory | (6,484) | (6,788) |
| | $ 80,570 | $ 74,146 |

**(8) Debt**

Long-term debt consists of the following:

| | July 1, 2007 | December 31, 2006 |
|---|---|---|
| | (Unaudited) | |
| Revolving credit facility | $ 18,000 | $ 5,000 |
| Senior notes | 30,000 | 55,000 |
| | 48,000 | 60,000 |
| Less current portion | | 5,000 |

| | | | | |
|---|---|---|---|---|
| | $ | 48,000 | $ | 55,000 |

In April 2007, the Company s Credit Agreement was amended and restated to: i) limit total borrowings at $50,000,000, with $50,000,000 of additional borrowings available upon lead bank approval, ii) extend the Credit Agreement through October 2009, iii) revise certain financial covenants providing more flexibility in the Company s financing structure, iv) increase the Company s interest rate structure, and v) add a security interest in the Company s accounts receivable, inventory and equipment. Other terms of the Credit Agreement remained substantially unchanged.

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The Company also amended the Senior Notes in April 2007 to enable a portion of their repayment, revise certain financial covenants, modify the June 30, 2014 principal payment to June 30, 2012, increase the Company s fixed interest rates and among other things, add a security interest in the Company s accounts receivable, inventory and equipment. Other terms of the Senior Notes remained substantially unchanged. As a result of the aforementioned modifications, the Company deferred $849,000 of loan costs, which are included in other assets in the consolidated balance sheets.

After the aforementioned modifications, the Company s principal commitment under the revolving credit facility is due in 2009, while the Company s principal commitment under the Senior Notes is $4,100,000, $15,000,000 and $10,900,000 due in 2009, 2011 and 2012, respectively.

**(9) Segment Data**

The Company is organized into two business groups, the Industrial Group and the Electronics Group. The Industrial Group is one reportable business segment, while the Electronics Group includes two reportable business segments, Aerospace & Defense and Test & Measurement. There was no intersegment net revenue recognized in any of the periods presented. The following table presents financial information for the reportable segments of the Company (in thousands):

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | July 1, 2007 | June 30, 2006 | July 1, 2007 | June 30, 2006 |
| | (Unaudited) | | (Unaudited) | |
| Net revenue from unaffiliated customers: | | | | |
| Industrial Group | $ 73,472 | $ 98,454 | $ 152,591 | $ 190,952 |
| Aerospace & Defense | 29,380 | 21,917 | 49,051 | 47,927 |
| Test & Measurement | 13,395 | 11,862 | 26,044 | 23,349 |
| Electronics Group | 42,775 | 33,779 | 75,095 | 71,276 |
| | $ 116,247 | $ 132,233 | $ 227,686 | $ 262,228 |
| Gross profit: | | | | |
| Industrial Group | $ 3,749 | $ 4,491 | $ 9,069 | $ 10,439 |
| Aerospace & Defense | 777 | 3,347 | 3,932 | 7,301 |
| Test & Measurement | 3,175 | 2,596 | 6,707 | 5,311 |
| Electronics Group | 3,952 | 5,943 | 10,639 | 12,612 |
| | $ 7,701 | $ 10,434 | $ 19,708 | $ 23,051 |
| Operating income (loss): | | | | |
| Industrial Group | $ 1,468 | $ 2,127 | $ 4,351 | $ 5,330 |
| Aerospace & Defense | (2,590) | 348 | (2,887) | 1,137 |
| Test & Measurement | 765 | 42 | 1,397 | 248 |
| Electronics Group | (1,825) | 390 | (1,490) | 1,385 |
| General, corporate and other | (2,843) | (2,244) | (5,799) | (4,236) |
| | $ (3,200) | $ 273 | $ (2,938) | $ 2,479 |

**(10) Commitments and Contingencies**

The Company bears insurance risk as a member of a group captive insurance entity for certain general liability, automobile and workers compensation insurance programs and a self-insured employee health program. The Company records estimated liabilities for its insurance programs based on information provided by the third-party plan administrators, historical claims experience, expected costs of claims incurred but not paid, and expected costs to settle unpaid claims. The Company monitors its estimated insurance-related liabilities on a quarterly basis. As facts change, it may become necessary to make adjustments that could be material to the Company s consolidated results of operations and financial condition. The Company believes that its present insurance coverage and level of accrued liabilities are adequate.

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The Company is involved in certain litigation and contract issues arising in the normal course of business. While the outcome of these matters cannot, at this time, be predicted in light of the uncertainties inherent therein, management does not expect that these matters will have a material adverse effect on the consolidated financial position or results of operations of the Company, excluding the aforementioned pending major customer bankruptcy proceedings.

As of July 1, 2007, the Company had outstanding purchase commitments of approximately $27,773,000, primarily for the acquisition of inventory and manufacturing equipment. As of July 1, 2007, the Company also had outstanding letters of credit approximating $2,794,000 primarily under a captive insurance program.

**(11) Income Taxes**

In June 2006, the FASB issued FASB Interpretation No. 48 (FIN 48), Accounting for Uncertainty in Income Taxes, an interpretation of FASB Statement No. 109. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with FASB Statement No. 109, Accounting for Income Taxes. Specifically, FIN 48 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return and also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. The Company adopted the provisions of FIN 48 on January 1, 2007. The impact of the Company s tax positions reassessment in accordance with the requirements of FIN 48 was not significant.

Upon the adoption of FIN 48 as of January 1, 2007, the estimated value of the Company s uncertain tax positions approximated $1,000,000 applicable to unrecognized net tax benefits. If the Company s positions are sustained by the taxing authority in favor of the Company, the entire balance would reduce the Company s effective tax rate. The Company does not expect any reasonably possible material changes to the estimated amount of liability associated with its uncertain tax positions through July 2008. As of July 1, 2007, there have been no significant changes to the liability for uncertain tax positions. The Company recognizes accrued interest and penalties related to uncertain tax positions in income tax expense. As of July 1, 2007, the Company had accrued approximately $300,000 for the payment of tax-related interest and penalties. The liability for uncertain tax positions including interest and penalties is carried in other liabilities in the consolidated balance sheets.

The Company s effective tax rate for the three and six months ended July 1, 2007 was 45%. The Company s effective tax rate for the three and six months ended June 30, 2006 was 45% and 17%, respectively. Reconciling items between the federal statutory income tax rate of 34% and the effective tax rate include state and foreign income taxes and certain other permanent differences.

The Company files income tax returns in the U.S. federal jurisdiction, and various state and foreign jurisdictions. The Internal Revenue Service (IRS) is not currently examining the Company s U.S. income tax returns for 2003 through 2007, for which the statute has yet to expire. In addition, open tax years related to state and foreign jurisdictions remain subject to examination but are not considered material.

The Company s Mexican subsidiary is currently under a routine audit by the Mexican Servicio de Administracion Tributaria (SAT), the Mexican taxing authority, for the periods from May 27, 2004 through July 20, 2007. Proposed audit adjustments, if any, could significantly impact the Company s operating results.

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**(12) Employee Benefit Plans**

Pension (benefit) expense consisted of the following (in thousands):

| | Three Months Ended | | Six Months Ended | |
|---|---|---|---|---|
| | July 1, 2007 | June 30, 2006 | July 1, 2007 | June 30, 2006 |
| | (Unaudited) | | (Unaudited) | |
| Service cost | $ 28 | $ 25 | $ 56 | $ 49 |
| Interest cost on projected benefit obligation | 548 | 538 | 1,096 | 1,090 |
| Net amortizations, deferrals and other costs | 51 | 110 | 102 | 244 |
| Expected return on plan assets | (775) | (698) | (1,550) | (1,380) |
| | $ (148) | $ (25) | $ (296) | $ 3 |

**(13) Foreign Currency Translation**

The functional currency for the Company s Mexican subsidiary is the Mexican peso. Assets and liabilities are translated at current rates of exchange and income and expense items are translated at the weighted average exchange rate for the period. The resulting translation adjustments are recorded in other comprehensive loss as a separate component of stockholders equity. Total comprehensive loss for the three and six months ended July 1, 2007 was $1,721,000 and $2,674,000 respectively, including foreign currency translation adjustments of $580,000 and $128,000, respectively. For the three and six months ended July 1, 2007, other income, net includes foreign currency transaction losses of $61,000 and $46,000, respectively. Similar amounts for 2006 were not significant.

**(14) Subsequent Event**

On July 24, 2007, the Company announced that Sypris Technologies, Inc., a wholly-owned subsidiary, has entered into a comprehensive settlement agreement with Dana to resolve all outstanding disputes and enter into a new long-term supply contract. Dana filed a motion for an order approving the settlement agreement with the court in the Southern District of New York. The motion was heard by the court on August 7, 2007 and approved.

The agreement provides for Dana and the Company to (i) enter into a new, long-term master supply agreement in lieu of the three existing supply contracts, (ii) exchange production of certain non-core components, (iii) rebalance production among Company plants to reduce costs for both parties, and (iv) cease all litigation with regard to prior contract disputes, including the release of Dana from certain committed but undelivered production volumes. In addition, Dana will provide the Company with an allowed general unsecured claim in the amount of $89,900,000, a significant portion of which is expected to be deferred.

The new master supply agreement will run through 2014 and provides Dana with enhanced pricing for certain products beginning in 2008, and improved coverage in the areas of quality and warranty, among others.

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**ITEM 2. MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

**Results of Operations**

The tables presented below, which compare our results of operations for the three and six month periods from 2007 to 2006, presents the results for each period, the change in those results from 2007 to 2006 in both dollars and percentage change and the results for each period as a percentage of net revenue. The columns present the following:

The first two data columns in the table show the absolute results for each period presented.

The columns entitled Year Over Year Change and Year Over Year Percentage Change show the change in results, both in dollars and percentages. These two columns show favorable changes as positive and unfavorable changes as negative. For example, when our net revenue increases from one period to the next, that change is shown as a positive number in both columns. Conversely, when expenses increase from one period to the next, that change is shown as a negative number in both columns.

The last two columns in the table show the results for each period as a percentage of net revenue. In these two columns, the cost of sales and gross profit for each are given as a percentage of that segment s net revenue. These amounts are shown in italics.

In addition, as used in the table, NM means not meaningful.

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**Three Months Ended July 1, 2007 Compared to Three Months Ended June 30, 2006**

| | Three Months Ended, July 1, 2007 | Three Months Ended, June 30, 2006 | Year Over Year Change Favorable (Unfavorable) | Year Over Year Percentage Change Favorable (Unfavorable) | Results as Percentage of Net Revenue for the Three Months Ended July 1, 2007 | Results as Percentage of Net Revenue for the Three Months Ended June 30, 2006 |
|---|---|---|---|---|---|---|
| | (in thousands, except percentage data) | | | | | |
| Net revenue: | | | | | | |
| Industrial Group | $ 73,472 | $ 98,454 | $ (24,982) | (25.4)% | 63.2% | 74.4% |
| Aerospace & Defense | 29,380 | 21,917 | 7,463 | 34.1 | 25.3 | 16.6 |
| Test & Measurement | 13,395 | 11,862 | 1,533 | 12.9 | 11.5 | 9.0 |
| Electronics Group | 42,775 | 33,779 | 8,996 | 26.6 | 36.8 | 25.6 |
| Total | 116,247 | 132,233 | (15,986) | (12.1) | 100.0 | 100.0 |
| Cost of sales: | | | | | | |
| Industrial Group | 69,723 | 93,963 | 24,240 | 25.8 | *94.9* | *95.4* |
| Aerospace & Defense | 28,603 | 18,570 | (10,033) | (54.0) | *97.4* | *84.7* |
| Test & Measurement | 10,220 | 9,266 | (954) | (10.3) | *76.3* | *78.1* |
| Electronics Group | 38,823 | 27,836 | (10,987) | (39.5) | *90.8* | *82.4* |
| Total | 108,546 | 121,799 | 13,253 | | | |