PHOTRONICS INC
Form 10-Q
June 05, 2013

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended April 28, 2013
OR

o 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 0-15451

PHOTRONICS, INC.
(Exact name of registrant as specified in its charter)

Connecticut (State or other jurisdiction of incorporation or organization)	06-0854886 (IRS Employer Identification No.)
15 Secor Road, Brookfield, Connecticut (Address of principal executive offices)	06804 (Zip Code)
Registrant's telephone number, including area code	(203) 775-9000

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 periods 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 Web site, 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 definitions of “large accelerated filer," "accelerated filer” and “smaller reporting company” in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer o	Accelerated Filer x	Non-Accelerated Filer o	Smaller Reporting Company o

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at May 31, 2013
Common Stock, $0.01 par value	60,967,777 Shares

Forward-Looking Statements

The Private Securities Litigation Reform Act of 1995 provides a "safe harbor" for forward-looking statements made by or on behalf of Photronics, Inc. ("Photronics" or the "Company"). These statements are based on management's beliefs, as well as assumptions made by, and information currently available to, management. Forward-looking statements may be identified by words like "expect", "anticipate", "believe", "plan", "projects", and similar expressions, or the negative of such terms, or other comparable terminology. All forward-looking statements involve risks and uncertainties that are difficult to predict. In particular, any statement contained in this quarterly report on Form 10-Q or in other documents filed with the Securities and Exchange Commission, in press releases or in the Company's communications and discussions with investors and analysts in the normal course of business through meetings, phone calls, or conference calls regarding, among other things, the consummation and benefits of future transactions and acquisitions, expectations with respect to future sales, financial performance, operating efficiencies, or product expansion, are subject to known and unknown risks, uncertainties, and contingencies, many of which are beyond the control of the Company. Various factors may cause actual results, performance, or achievements to differ materially from anticipated results, performance, or achievements expressed or implied by forward-looking statements. Factors that might affect forward-looking statements include, but are not limited to, overall economic and business conditions; economic and political conditions in international markets; the demand for the Company's products; competitive factors in the industries and geographic markets in which the Company competes; federal, state and international tax requirements (including tax rate changes, new tax laws and revised tax law interpretations); interest rate and other capital market conditions, including changes in the market price of the Company's securities; foreign currency exchange rate fluctuations; changes in technology; the timing, impact, and other uncertainties of future transactions and acquisitions, divestitures and joint ventures as well as decisions the Company may make in the future regarding the Company’s business, capital and organizational structure and other matters; the seasonal and cyclical nature of the semiconductor and flat panel display industries; management changes; damage or destruction to the Company's facilities, or the facilities of its customers or suppliers, by natural disasters, labor strikes, political unrest, or terrorist activity; the ability of the Company to (i) place new equipment in service on a timely basis; (ii) obtain additional financing; (iii) achieve anticipated synergies and cost savings; (iv) fully utilize its tools; (v) achieve desired yields, pricing, product mix, and market acceptance of its products and (vi) obtain necessary export licenses. Any forward-looking statements should be considered in light of these factors. Accordingly, there is no assurance that the Company's expectations will be realized. The Company does not assume responsibility for the accuracy and completeness of the forward-looking statements and does not assume an obligation to provide revisions to any forward-looking statements, except as otherwise required by securities laws.

PHOTRONICS, INC.
AND SUBSIDIARIES

INDEX

PART I.	FINANCIAL INFORMATION	Page
Item 1.	Condensed Consolidated Financial Statements	
	Condensed Consolidated Balance Sheets at April 28, 2013 and October 28, 2012	4
	Condensed Consolidated Statements of Income for the Three and Six Months Ended April 28, 2013 and April 29, 2012	5
	Condensed Consolidated Statements of Comprehensive Income (Loss) for the Three and Six Months Ended April 28, 2013 and April 29, 2012	6
	Condensed Consolidated Statements of Cash Flows for the Six Months Ended April 28, 2013 and April 29, 2012	7
	Notes to Condensed Consolidated Financial Statements	8
Item 2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	20
Item 3.	Quantitative and Qualitative Disclosures about Market Risk	25
Item 4.	Controls and Procedures	26
PART II.	OTHER INFORMATION	
Item 1A.	Risk Factors	26
Item 6.	Exhibits	27

Index

PART I. FINANCIAL INFORMATION

Item 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

PHOTRONICS, INC. AND SUBSIDIARIES
Condensed Consolidated Balance Sheets
(in thousands, except per share amounts)
(unaudited)

	April 28, 2013	October 28, 2012
ASSETS		
Current assets:		
Cash and cash equivalents	$210,552	$218,043
Accounts receivable, net of allowance of $3,468 in 2013 and $3,902 in 2012	82,715	75,685
Inventories	18,585	17,702
Other current assets	9,525	8,364
Total current assets	321,377	319,794
Property, plant and equipment, net	410,757	380,808
Investment in joint venture	93,050	93,252
Intangible assets, net	36,776	37,384
Deferred income taxes	11,169	11,395
Other assets	7,730	6,601
Total assets	$880,859	$849,234
LIABILITIES AND EQUITY		
Current liabilities:		
Current portion of long-term borrowings	$10,473	$7,781
Accounts payable	79,432	53,031
Accrued liabilities	24,493	24,701
Total current liabilities	114,398	85,513
Long-term borrowings	169,348	168,956
Other liabilities	9,665	8,764
Total liabilities	293,411	263,233
Commitments and contingencies		
Equity:		
Preferred stock, $0.01 par value, 2,000 shares authorized, none issued and outstanding	-	-
Common stock, $0.01 par value, 150,000 shares authorized, 60,598 shares issued and outstanding at April 28, 2013 and 60,213 at October 28, 2012	606	602
Additional paid-in capital	496,204	493,411
Retained earnings	48,660	41,473
Accumulated other comprehensive income	11,416	15,900
Total Photronics, Inc. shareholders' equity	556,886	551,386

Noncontrolling interests	30,562	34,615
Total equity	587,448	586,001
Total liabilities and equity	$880,859	$849,234

See accompanying notes to condensed consolidated financial statements.

Index

PHOTRONICS, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Income
(in thousands, except per share amounts)
(unaudited)

	Three Months Ended		Six Months Ended	
	April 28, 2013	April 29, 2012	April 28, 2013	April 29, 2012
Net sales	$106,680	$117,451	$206,519	$229,605
Costs and expenses:				
Cost of sales	(81,891)	(87,590)	(160,632)	(174,286)
Selling, general and administrative	(12,151)	(12,201)	(23,218)	(23,526)
Research and development	(4,556)	(4,441)	(9,395)	(8,885)
Consolidation, restructuring and related charges	-	(58)	-	(1,176)
Operating income	8,082	13,161	13,274	21,732
Other income (expense):				
Interest expense	(1,909)	(1,795)	(3,796)	(3,575)
Interest and other income (expense), net	993	827	2,289	2,198
Income before income tax provision	7,166	12,193	11,767	20,355
Income tax provision	(1,724)	(2,663)	(3,466)	(5,984)
Net income	5,442	9,530	8,301	14,371
Net income attributable to noncontrolling interests	(579)	(712)	(1,114)	(1,285)
Net income attributable to Photronics, Inc. shareholders	$4,863	$8,818	$7,187	$13,086
Earnings per share:				
Basic	$0.08	$0.15	$0.12	$0.22
Diluted	$0.08	$0.14	$0.12	$0.21
Weighted-average number of common shares outstanding:				
Basic	60,493	60,086	60,385	59,952
Diluted	61,501	76,590	61,298	76,472

See accompanying notes to condensed consolidated financial statements.

Index

PHOTRONICS, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Comprehensive Income (Loss)
(in thousands)
(unaudited)

	Three Months Ended April 28, 2013	Three Months Ended April 29, 2012	Six Months Ended April 28, 2013	Six Months Ended April 29, 2012
Net income	$5,442	$9,530	$8,301	$14,371
Other comprehensive income (loss), net of tax of $0:				
Foreign currency translation adjustments	(13,104)	741	(4,963)	(412)
Amortization of cash flow hedge	32	32	64	64
Other	14	-	10	-
Other comprehensive income (loss)	(13,058)	773	(4,889)	(348)
Comprehensive income (loss)	(7,616)	10,303	3,412	14,023
Less: comprehensive income (loss) attributable to noncontrolling interests	(82)	1,795	682	2,642
Comprehensive income (loss) attributable to Photronics, Inc. shareholders	$(7,534)	$8,508	$2,730	$11,381

See accompanying notes to condensed consolidated financial statements.

Index

PHOTRONICS, INC. AND SUBSIDIARIES
Condensed Consolidated Statements of Cash Flows

(in thousands)

(unaudited)

	Six Months Ended April 28, 2013	Six Months Ended April 29, 2012
Cash flows from operating activities:		
Net income	$8,301	$14,371
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	37,490	44,135
Consolidation, restructuring and related charges	-	262
Changes in assets and liabilities:		
Accounts receivable	(8,086)	(2,829)
Inventories	(1,063)	1,622
Other current assets	(1,572)	(698)
Accounts payable, accrued liabilities and other	864	5,536
Net cash provided by operating activities	35,934	62,399
Cash flows from investing activities:		
Purchases of property, plant and equipment	(31,866)	(67,626)
Investment in joint venture	-	(5,899)
Other	(2,822)	(1,600)
Net cash used in investing activities	(34,688)	(75,125)
Cash flows from financing activities:		
Proceeds from long-term borrowings	-	25,000
Repayments of long-term borrowings	(3,319)	(2,343)
Repurchase of common stock by subsidiary	(4,190)	(7,577)
Proceeds from share-based arrangements	588	431
Payments of deferred financing fees	(40)	(198)
Net cash provided by (used in) financing activities	(6,961)	15,313
Effect of exchange rate changes on cash and cash equivalents	(1,776)	(555)
Net increase (decrease) in cash and cash equivalents	(7,491)	2,032
Cash and cash equivalents at beginning of period	218,043	189,928
Cash and cash equivalents at end of period	$210,552	$191,960
Supplemental disclosure of non-cash information:		
Accrual for property, plant and equipment purchased during the period	$(32,502)	$(2,549)
Deposit related to facility purchase	-	2,000

See accompanying notes to condensed consolidated financial statements.

Index

PHOTRONICS, INC. AND SUBSIDIARIES
Notes to Condensed Consolidated Financial Statements
Three Months and Six Months Ended April 28, 2013 and April 29, 2012
(unaudited)
(in thousands, except share amounts)

NOTE 1 - BASIS OF FINANCIAL STATEMENT PRESENTATION

Photronics, Inc. and its subsidiaries ("Photronics" or “the Company") is one of the world's leading manufacturers of photomasks, which are high precision photographic quartz plates containing microscopic images of electronic circuits. Photomasks are a key element in the manufacture of semiconductors and flat panel displays ("FPDs"), and are used as masters to transfer circuit patterns onto semiconductor wafers and flat panel substrates during the fabrication of integrated circuits ("ICs") and a variety of FPDs and, to a lesser extent, other types of electrical and optical components. The Company currently operates principally from eight manufacturing facilities, two of which are located in Europe, two in Taiwan, one in Korea, and three in the United States.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America for annual financial statements. In the opinion of management, all adjustments considered necessary for a fair presentation have been included. Operating results for the interim period are not necessarily indicative of the results that may be expected for the fiscal year ending November 3, 2013. For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the year ended October 28, 2012.

NOTE 2 - CHANGES IN EQUITY

The following tables set forth the Company's consolidated changes in equity for the three and six month periods ended April 28, 2013 and April 29, 2012:

Three Months Ended April 28, 2013
Photronics, Inc. Shareholders

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Non-controlling Interests	Total Equity
Balance at January 28, 2013	60,362	$603	$494,984	$43,797	$ 23,812	$30,645	$593,841
Net income	-	-	-	4,863	-	579	5,442
Other comprehensive loss	-	-	-	-	(12,396)	(662)	(13,058)
Sale of common stock through employee stock	212	2	281	-	-	-	283

option and purchase plans							
Restricted stock awards vesting and expense	24	1	340	-	-	-	341
Share-based compensation expense	-	-	599	-	-	-	599
Balance at April 28, 2013	60,598	$606	$496,204	$48,660	$ 11,416	$30,562	$587,448

8

Index

Three Months Ended April 29, 2012

Photronics, Inc. Shareholders

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Non-controlling Interests	Total Equity
Balance at January 30, 2012	60,015	$600	$488,674	$17,873	$ 8,773	$48,526	$564,446
Net income	-	-	-	8,818	-	712	9,530
Other comprehensive income (loss)	-	-	-	-	(310)	1,083	773
Sale of common stock through employee stock option and purchase plans	81	1	94	-	-	-	95
Restricted stock awards vesting and expense	10	-	210	-	-	-	210
Share-based compensation expense	-	-	506	-	-	-	506
Repurchase of common stock by subsidiary	-	-	866	-	(32)	(7,516)	(6,682)
Balance at April 29, 2012	60,106	$601	$490,350	$26,691	$ 8,431	$42,805	$568,878

Six Months Ended April 28, 2013

Photronics, Inc. Shareholders

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Non-controlling Interests	Total Equity
Balance at October 29, 2012	60,213	$602	$493,411	$41,473	$ 15,900	$34,615	$586,001
Net income	-	-	-	7,187	-	1,114	8,301
Other comprehensive loss	-	-	-	-	(4,457)	(432)	(4,889)
Sale of common stock through	289	3	390	-	-	-	393

employee stock option and purchase plans							
Restricted stock awards vesting and expense	96	1	610	-	-	-	611
Share-based compensation expense	-	-	1,214	-	-	-	1,214
Repurchase of common stock by subsidiary	-	-	579	-	(27)	(4,735)	(4,183)
Balance at April 28, 2013	60,598	$606	$496,204	$48,660	$ 11,416	$30,562	$587,448

9

Index

Six Months Ended April 29, 2012
Photronics, Inc. Shareholders

	Common Stock Shares	Common Stock Amount	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income	Non-controlling Interests	Total Equity
Balance at October 31, 2011	59,651	$597	$486,674	$13,605	$ 10,171	$48,709	$559,756
Net income	-	-	-	13,086	-	1,285	14,371
Other comprehensive income (loss)	-	-	-	-	(1,705)	1,357	(348)
Sale of common stock through employee stock option and purchase plans	203	2	237	-	-	-	239
Restricted stock awards vesting and expense	75	-	452	-	-	-	452
Share-based compensation expense	-	-	919	-	-	-	919
Common stock warrants exercised	177	2	1,051	-	-	-	1,053
Repurchase of common stock by subsidiary	-	-	1,017	-	(35)	(8,546)	(7,564)
Balance at April 29, 2012	60,106	$601	$490,350	$26,691	$ 8,431	$42,805	$568,878

NOTE 3 - PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment consists of the following:

	April 28, 2013	October 28, 2012
Land	$ 8,506	$ 8,538
Buildings and improvements	102,207	101,409
Machinery and equipment	1,180,839	1,197,854
Leasehold improvements	4,128	5,854
Furniture, fixtures and office equipment	12,885	13,484
Construction in progress	84,362	26,642
	1,392,927	1,353,781

Less accumulated depreciation and amortization	982,170	972,973
	$ 410,757	$ 380,808

Equipment under capital leases are included in above property, plant and equipment as follows:

	April 28, 2013	October 28, 2012
Machinery and equipment	$ 21,327	$ 21,327
Construction in progress	6,916	-
	28,243	21,327
Less accumulated amortization	3,824	2,758
	$ 24,419	$ 18,569

Index

Depreciation expense for property, plant and equipment (excluding equipment under capital leases) was $16.1 million and $33.1 million for the three and six month periods ended April 28, 2013, respectively, and $18.7 million and $37.1 million for the three and six month periods ended April 29, 2012, respectively. Amortization expense for equipment under capital leases was $0.5 million and $1.0 million for the three and six month periods ended April 28, 2013, respectively and $1.2 million and $3.8 million for the three and six month periods ended April 29, 2012, respectively.

NOTE 4 - JOINT VENTURE, TECHNOLOGY LICENSE AND OTHER AGREEMENTS WITH MICRON TECHNOLOGY, INC.

In May 2006, Photronics and Micron Technology, Inc. ("Micron") entered into the MP Mask joint venture (“MP Mask”), which develops and produces photomasks for leading-edge and advanced next generation semiconductors. As part of the formation of the joint venture, Micron contributed its existing photomask technology center located in Boise, Idaho, (headquarters of MP Mask) and Photronics invested $135 million in exchange for a 49.99% interest in MP Mask (to which $64.2 million of the original investment was allocated), a license for photomask technology of Micron, and certain supply agreements.

This joint venture is a variable interest entity ("VIE") (as that term is defined in the Accounting Standards Codification ("ASC") because all costs of the joint venture are passed on to the Company and Micron through purchase agreements they have entered into with the joint venture, and it is dependent upon the Company and Micron for any additional cash requirements. On a quarterly basis the Company reassesses whether its interest in MP Mask gives it a controlling financial interest in this VIE. The purpose of this quarterly reassessment is to identify the primary beneficiary (which is defined in the ASC as the entity that consolidates a VIE) of the VIE. As a result of the reassessment in the current quarter, the Company determined that Micron is still the primary beneficiary of the VIE, by virtue of its tie-breaking voting rights within MP Mask’s Board of Managers, thereby giving it the power to direct the activities of MP Mask that most significantly impact its economic performance, including its decision making authority in the ordinary course of business and its purchasing the majority of products produced by the VIE.

The Company has utilized MP Mask for both high-end IC photomask production and research and development purposes. MP Mask charges its variable interest holders based on their actual usage of its facility. MP Mask separately charges for any research and development activities it engages in at the requests of its owners. The Company recorded cost of sales of $3.5 million and $5.4 million and research and development expenses of $0.2 million and $0.5 million during the three and six month periods ended April 28, 2013. Cost of sales of $2.1 million and $4.1 million and research and development expenses of $0.2 million and $0.5 million were recorded during the three and six month periods ended April 29, 2012. As of April 28, 2013 and October 28, 2012, the Company owed MP Mask $5.5 million and $6.4 million, respectively, and had a receivable from Micron of $7.9 million and $9.0 million, respectively, both primarily related to the aforementioned supply agreements.

MP Mask is governed by a Board of Managers, appointed by Micron and the Company. Since MP Mask's inception, Micron, as a result of its majority ownership, has held majority voting power on the Board of Managers. The voting power held by each party is subject to change as ownership interests change. Under the MP Mask joint venture operating agreement, the Company may be required to make additional capital contributions to MP Mask up to the maximum amount defined in the operating agreement. However, should the Board of Managers determine that further additional funding is required, MP Mask shall pursue its own financing. If MP Mask is unable to obtain its own financing, it may request additional capital contributions from the Company. Should the Company choose not to make a requested contribution to MP Mask, its ownership percentage may be reduced. The Company increased its investment in the MP Mask joint venture by $5.4 million and $5.8 million during the three and six month periods ended April 29, 2012, respectively. These investments were primarily related to capital calls made by the joint venture. The Company did not make any capital contributions to the joint venture during the six month period ended April 28, 2013, and did not receive any distributions from the joint venture during the six month periods ended April

28, 2013 and April 29, 2012.

The Company's investment in the VIE, which represents its maximum exposure to loss, was $93.1 million at April 28, 2013, and $93.3 million at October 28, 2012. These amounts are reported in the Company's condensed consolidated balance sheets as "Investment in joint venture". The Company recorded a loss from its investment in the VIE of $0.2 million in the six month period ended April 28, 2013, and recorded no income from its investment in the three month period ended April 28, 2013, or in the three or six month periods ended April 29, 2012. Income from the VIE is included in "Interest and other income (expense), net" in the condensed consolidated statements of income.

In the second quarter of fiscal 2012 the Company paid $35 million to Micron in connection with its purchase of the U.S. nanoFab facility, which it had been leasing from Micron under a lease which ran through December 31, 2014.

Index

NOTE 5 - LONG-TERM BORROWINGS

Long-term borrowings consist of the following:

	April 28, 2013		October 28, 2012	
3.25% convertible senior notes due on April 1, 2016	$	115,000	$	115,000
Variable rate term loan, maturing March 1, 2017		22,500		23,750
5.5% convertible senior notes due on October 1, 2014		22,054		22,054
3.09% capital lease obligation payable through March 2016		13,106		15,175
Capital lease obligation payable through 2018		6,916		-
4.75% financing loan with customer		245		758
		179,821		176,737
Less current portion		10,473		7,781
	$	169,348	$	168,956

In February 2013 the Company entered into a five year capital lease to fund the purchase of a high-end lithography tool. The principal amount of the lease, which is currently estimated to be approximately $27 million, will be determined by the Japanese yen exchange rate to the U.S. dollar as progress payments are made on the tool. The interest rate will be fixed, based on the five year interest rate swap plus a spread, upon acceptance of the tool which is expected to occur in the fourth quarter of fiscal year 2013. Progress payments totaling $6.9 million have been made by the lessor through April 28, 2013, and are included in the Company's long-term borrowings as a non-cash capital lease obligation as of that date. Accordingly, this amount was excluded from both operating and financing cash activities.

In March 2012 the Company, in connection with its purchase of the U.S. nanoFab facility (see Note 4 for further discussion), amended its credit facility ("the credit facility") to include the addition of a $25 million variable rate (2.5% at April 28, 2013) term loan maturing in March 2017 with minimum quarterly principal payments of $0.6 million (quarterly payments commenced in June 2012 and are based on a ten year repayment period). The amendment also included a twenty-five basis point reduction in the interest rate charged on any borrowings under the credit facility.

The credit facility bears interest (2.5% at April 28, 2013) based on the Company's total leverage ratio, at LIBOR plus a spread, as defined in the credit facility. The credit facility is secured by substantially all of the Company's assets located in the United States, as well as common stock the Company owns in certain of its foreign subsidiaries, and is subject to the following financial covenants: minimum fixed charge ratio, total leverage ratio and minimum unrestricted cash balance. As of April 28, 2013, the Company had no outstanding borrowings under the credit facility and $30 million was available for borrowing.

In March 2011 the Company issued through a private offering, pursuant to Rule 144A under the Securities Act of 1933, as amended, $115 million aggregate principal amount of 3.25% convertible senior notes. The notes mature on April 1, 2016, and note holders may convert each $1,000 principal amount of notes to 96.3879 shares of common stock (equivalent to an initial conversion price of $10.37 per share of common stock) at any time prior to the close of business on the second scheduled trading day immediately preceding April 1, 2016. The conversion rate is subject to adjustment upon the occurrence of certain events, which are described in the indenture dated March 28, 2011. The Company is not required to redeem the notes prior to their maturity date. Interest on the notes accrues in arrears, and is paid semiannually through the notes' maturity date. Interest payments on the notes commenced on October 1, 2011.

The net proceeds of the notes were approximately $110.7 million, which were used, in part, to acquire $35.4 million of the Company's 5.5% convertible senior notes which were to mature on October 1, 2014, and to repay, in full, its then outstanding obligations under capital leases of $19.8 million.

In September 2009 the Company issued, through a public offering, $57.5 million aggregate principal amount of 5.5% convertible senior notes, which were to mature on October 1, 2014. Under the terms of the offering, the note holders could convert each $1,000 principal amount of notes to 196.7052 shares of common stock (equivalent to an initial conversion price of $5.08 per share of common stock) on, or before, September 30, 2014. The conversion rate is subject to adjustment upon the occurrence of certain events which are described in the indenture dated September 16, 2009. The Company is not required to redeem the notes prior to their maturity. The net proceeds of this offering were approximately $54.9 million, which were used to reduce amounts outstanding under the Company's credit facility. A portion of the notes from this issuance having an aggregate principal amount of $35.4 million were acquired by the Company during fiscal year 2011.

Index

In April 2011 the Company entered into a five year, $21.2 million capital lease for manufacturing equipment. Payments under the lease, which bears interest at 3.09%, are $0.4 million per month through March 2016. The lease agreement provides that the Company must maintain the equipment in good working order, and includes a cross default with cross acceleration provision related to certain non-financial covenants incorporated in the Company's credit facility agreement. As of April 28, 2013, the total amount payable through the end of the lease term was $13.7 million, of which $13.1 million represented principal and $0.6 million represented interest.

In January 2010 the Company borrowed $3.7 million from a customer to purchase manufacturing equipment. This loan bears interest at 4.75% and is primarily being repaid with product supplied to the customer. Product valued at $0.3 million and $0.5 million was shipped to the customer and applied against the loan during the three and six month periods ended April 28, 2013, respectively, and product valued at $0.2 million and $0.5 million was applied against the loan in the respective prior year periods. The Company estimates that the loan will be fully repaid in fiscal 2013.

NOTE 6 - COMMON STOCK WARRANTS

In September 2009 the Company entered into two warrant agreements with Intel Capital Corporation to purchase a total of 750,000 shares of the Company's common stock. Under one warrant agreement 500,000 shares of the Company's common stock can be purchased at an exercise price of $4.15 per share and under the second warrant agreement 250,000 shares of the Company's common stock can be purchased at an exercise price of $5.08 per share. The warrant agreements expire in September 2014. Also in September 2009, the Company and Intel Corporation entered into an agreement to share technical and operations information regarding the development of the Company's products, the capabilities of the Company's photomask manufacturing lines and the alignment of photomask toolsets. Intel Capital Corporation also invested in the Company's convertible debt offering of September 2009. The warrants were recorded at their fair value on their date of grant, which was determined using the Black-Scholes option pricing model. As of April 28, 2013, none of the warrants issued to Intel Capital Corporation had been exercised.

NOTE 7 - SHARE-BASED COMPENSATION

In March 2007 shareholders approved a new share-based compensation plan ("Plan"), under which options, restricted stock, restricted stock units, stock appreciation rights, performance stock, performance units, and other awards based on, or related to, shares of the Company's common stock may be granted from shares authorized but unissued or shares previously issued and reacquired by the Company. A maximum of six million shares of common stock may be issued under the Plan. Awards may be granted to officers, employees, directors, consultants, advisors, and independent contractors of the Company or its subsidiaries. In the event of a change in control (as defined in the Plan), the vesting of awards may be accelerated. The Plan, aspects of which are more fully described below, prohibits further awards from being issued under prior plans. The Company incurred total share-based compensation costs for the three and six month periods ended April 28, 2013, of $0.9 million and $1.8 million, respectively, and $0.7 million and $1.4 million for the three and six month periods ended April 29, 2012, respectively. The Company received cash from option exercises of $0.3 million and $0.4 million for the three and six month periods ended April 28, 2013, respectively, and $0.1 million and $0.2 million for the three and six month periods ended April 29, 2012, respectively. No share-based compensation cost was capitalized as part of an asset and no related income tax benefits were recorded during the periods presented.

Stock Options

Option awards generally vest in one to four years, and have a ten-year contractual term. All incentive and non-qualified stock option grants have an exercise price equal to the market value of the underlying common stock on the date of grant. The grant date fair value of options are based on closing prices of the Company’s common stock on the dates of grant using the Black-Scholes option pricing model. Expected volatility is based on the historical volatility of the Company's stock. The Company uses historical option exercise behavior and employee termination data to estimate expected term, which represents the period of time that the options granted are expected to remain outstanding. The risk-free rate of return for the estimated term of the option is based on the U.S. Treasury yield curve in effect at the date of grant.

The weighted-average inputs and risk-free rate of return ranges used to calculate the grant date fair value of options issued during the three and six month periods ended April 28, 2013 and April 29, 2012, are presented in the following table.

Index

	Three Months Ended April 28, 2013		Three Months Ended April 29, 2012		Six Months Ended April 28, 2013		Six Months Ended April 29, 2012	
Expected volatility	84.5	%	102.2	%	99.6	%	102.1	%
Risk free rate of return	0.6	%	0.9	%	0.5% - 0.7	%	0.7% - 0.9	%
Dividend yield	N/A		N/A		N/A		N/A	
Expected term	4.3 years		4.3 years		4.3 years		4.3 years	

Information on outstanding and exercisable option awards as of April 28, 2013, is presented below.

Options	Shares		Weighted Average Exercise Price	Weighted Average Remaining Contractual Life		Aggregate Intrinsic Value
Outstanding at April 28, 2013	4,200,167	$	8.38	6.1 years	$	8,041
Exercisable at April 28, 2013	2,705,897	$	9.80	4.8 years	$	5,544

There were 20,000 share options granted during the three month period ended April 28, 2013, with a weighted-average grant date fair value of $4.07 per share, and there were 32,000 share options granted during the three month period ended April 29, 2012, with a grant date fair value of $4.72 per share. There were 584,000 share options granted during the six month period ended April 28, 2013, with a weighted-average grant date fair value of $3.99 per share and 524,500 share options granted during the six month period ended April 29, 2012, with a weighted-average grant date fair value of $4.47 per share. As of April 28, 2013, the total unrecognized compensation cost related to unvested option awards was approximately $4.6 million. That cost is expected to be recognized over a weighted-average amortization period of 2.6 years.

Restricted Stock

The Company periodically grants restricted stock awards. The restrictions on these awards lapse over a service period that has ranged from less-than-one to eight years. There were 5,000 restricted stock awards granted during the three month period ended April 28, 2013 with a weighted-average grant date fair value of $6.43 per share, and 209,500 restricted stock awards were issued during the six month period ended April 28, 2013, with a weighted-average grant date fair value of $5.48 per share. No restricted stock awards were granted during the three month period ended April 29, 2012, and 168,750 restricted stock awards were issued during the six month period ended April 29, 2012, with a weighted-average grant date fair value of $6.28 per share. As of April 28, 2013, the total compensation cost not yet recognized related to unvested restricted stock awards was approximately $1.8 million. That cost is expected to be recognized over a weighted-average amortization period of 2.1 years. As of April 28, 2013, there were 365,564 shares of restricted stock outstanding.

NOTE 8 - CONSOLIDATION, RESTRUCTURING AND RELATED CHARGES

In the first quarter of fiscal 2012 the Company ceased the manufacture of photomasks at its Singapore facility and, in connection therewith, recorded charges of $0.1 million and $1.2 million during the three and six month periods ended April 29, 2012, respectively. This restructuring, which was comprised primarily of employee termination costs, was substantially completed in fiscal 2012 at a cost of $1.4 million.

The following table sets forth the Company's restructuring reserve, primarily related to its Singapore facility, as of April 28, 2013 and April 29, 2012, and reflects the activity affecting the reserve for the three month period and six month periods then ended.

Index

	January 28, 2013	Three Months Ended April 28, 2013 Charges	Utilized	April 28, 2013	October 29, 2012	Six Months Ended April 28, 2013 Charges	Utilized	April 28, 2013
Employee terminations	$40	$-	$-	$40	$295	$-	$(255)	$40
	$40	$-	$-	$40	$295	$-	$(255)	$40

	January 30, 2012	Three Months Ended April 29, 2012 Charges	Utilized	April 29, 2012	October 31, 2011	Six Months Ended April 29, 2012 Charges	Utilized	April 29, 2012
Employee terminations	$419	$28	$(248)	$199	$-	$914	$(715)	$199
Asset write-downs	-	30	(30)	-	-	262	(262)	-
	$419	$58	$(278)	$199	$-	$1,176	$(977)	$199

NOTE 9 - INCOME TAXES

The effective income tax rates for the three and six month periods ended April 28, 2013 and April 29, 2012, differ from the U.S. statutory rate of 35% primarily due to foreign tax rate differences, as well as the existence of valuation allowances in jurisdictions with historical and continuing tax losses.

Unrecognized tax benefits related to uncertain tax positions were $3.9 million at April 28, 2013 and October 28, 2012, of which $1.9 million would favorably impact the Company's effective tax rate if recognized. Accrued interest and penalties related to unrecognized tax benefits were $0.1 million at April 28, 2013 and October 28, 2012. As of April 28, 2013, the total amount of unrecognized tax benefits is not expected to significantly increase or decrease in the next twelve months.

PKLT, the Company's FPD manufacturing facility in Taiwan, is accorded a tax holiday which commenced in 2012 and expires in 2017. The tax holiday had no dollar or per share effect in the three and six month periods ended April 28, 2013 or the three and six month periods ended April 29, 2012.

Index

NOTE 10 - EARNINGS PER SHARE

The calculation of basic and diluted earnings per share is presented below.

	Three Months Ended		Six Months Ended	
	April 28, 2013	April 29, 2012	April 28, 2013	April 29, 2012
Net income attributable to Photronics, Inc. shareholders	$4,863	$8,818	$7,187	$13,086
Effect of dilutive securities:				
Interest expense on convertible notes, net of related tax effects	-	1,542	-	3,084
Gain related to common stock warrants fair value adjustment	-	-	-	(94)
Earnings for diluted earnings per share	$4,863	$10,360	$7,187	$16,076
Weighted-average common shares computations:				
Weighted-average common shares used for basic earnings per share	60,493	60,086	60,385	59,952
Effect of dilutive securities:				
Share-based payment awards	766	829	726	830
Common stock warrants	242	252	187	267
Convertible notes	-	15,423	-	15,423
Potentially dilutive common shares	1,008	16,504	913	16,520
Weighted-average common shares used for diluted earnings per share	61,501	76,590	61,298	76,472
Basic earnings per share	$0.08	$0.15	$0.12	$0.22
Diluted earnings per share	$0.08	$0.14	$0.12	$0.21

The table below shows the outstanding weighted-average convertible notes and share-based payment awards that were excluded from the calculation of diluted earnings or loss per share because their exercise price exceeded the average market value of the common shares for the period or, under application of the treasury stock method, they were otherwise determined to be anti-dilutive.

	Three Months Ended		Six Months Ended	
	April 28, 2013	April 29, 2012	April 28, 2013	April 29, 2012
Convertible notes	15,423	-	15,423	-
Share-based payment awards	2,901	2,471	2,922	2,511
Total potentially dilutive shares excluded	18,324	2,471	18,345	2,511

Index

NOTE 11 - CHANGES IN ACCUMULATED OTHER COMPREHENSIVE INCOME BY COMPONENT

The following tables set forth the changes in the Company's accumulated other comprehensive income by component (net of tax of $0) for the three and six month periods ended April 28, 2013:

	Three Months Ended April 28, 2013			
	Foreign Currency Translation Adjustments	Amortization of Cash Flow Hedge	Other	Total
Balance at January 28, 2013	$25,152	$ (658)	$(682)	$23,812
Other comprehensive income (loss) before reclassifications	(13,104)	-	14	(13,090)
Amounts reclassified from other comprehensive income	-	32	-	32
Net current period other comprehensive income (loss)	(13,104)	32	14	(13,058)
Less: other comprehensive loss attributable to noncontrolling interests	662	-	-	662
Balance at April 28, 2013	$12,710	$ (626)	$(668)	$11,416

	Six Months Ended April 28, 2013			
	Foreign Currency Translation Adjustments	Amortization of Cash Flow Hedge	Other	Total
Balance at October 29, 2012	$17,241	$ (690)	$(651)	$15,900
Other comprehensive income (loss) before reclassifications	(4,963)	-	10	(4,953)
Amounts reclassified from other comprehensive income	-	64	-	64
Net current period other comprehensive income (loss)	(4,963)	64	10	(4,889)
Less: other comprehensive loss attributable to noncontrolling interests	432	-	-	432
Repurchase of common stock by subsidiary	-	-	(27)	(27)
Balance at April 28, 2013	$12,710	$ (626)	$(668)	$11,416

The amortization of the cash flow hedge is included in cost of sales in the condensed consolidated statements of income for all periods presented.

NOTE 12 – GEOGRAPHIC INFORMATION

The Company operates as a single operating segment as a manufacturer of photomasks, which are high precision quartz plates containing microscopic images of electronic circuits for use in the fabrication of ICs and FPDs. Geographic net sales are based primarily on where the Company's manufacturing facility is located.

Index

The Company's net sales by geographic area and for ICs and FPDs for the three and six month periods ended April 28, 2013 and April 29, 2012, and its long-lived assets by geographic area as of April 28, 2013 and October 28, 2012, are presented below.

	Three Months Ended		Six Months Ended	
	April 28, 2013	April 29, 2012	April 28, 2013	April 29, 2012
Net sales				
United States	$37,045	$37,128	$65,265	$68,698
Korea	32,332	41,514	66,304	83,426
Taiwan	27,425	27,680	55,819	54,159
Europe	9,388	10,384	17,988	20,734
All other	490	745	1,143	2,588
	$106,680	$117,451	$206,519	$229,605
IC	$82,164	$89,111	$156,588	$175,917
FPD	24,516	28,340	49,931	53,688
	$106,680	$117,451	$206,519	$229,605

	As of	
	April 28, 2013	October 28, 2012
Long-lived assets		
United States	$ 181,499	$ 177,614
Korea	147,649	120,628
Taiwan	71,319	72,185
Europe	10,252	10,262
All other	38	119
	$ 410,757	$ 380,808

The Company is typically impacted during its first fiscal quarter by the North American and European holiday periods, as some customers reduce their effective workdays and orders during these periods. Additionally, the Company can be impacted during its first or second quarter by the Asian New Year holiday period, which may also reduce customer orders.

NOTE 13 - FAIR VALUE MEASUREMENTS

The accounting framework for determining fair value includes a hierarchy for ranking the quality and reliability of the information used to measure fair value, which enables the reader of the financial statements to assess the inputs used to develop those measurements. The fair value hierarchy consists of three tiers as follows: Level 1, defined as quoted market prices in active markets for identical securities; Level 2, defined as inputs other than Level 1 that are observable, either directly or indirectly; and Level 3, defined as unobservable inputs that are not corroborated by market data.

The Company did not have any assets or liabilities measured at fair value, on a recurring or a nonrecurring basis, at April 28, 2013 or October 28, 2012.

Fair Value of Other Financial Instruments

The fair values of the Company's cash and cash equivalents (Level 1 measurements), accounts receivable, accounts payable, and certain other current assets and current liabilities (Level 2 measurements) approximate their carrying value due to their short-term maturities. The fair value of the Company's financing loan with a customer is a Level 2 measurement that approximates its carrying value due to its short-term maturity. The fair value of the Company's variable rate term loan is a Level 2 measurement and approximates its carrying value due to the variable nature of the underlying interest rates. The fair value of the Company's convertible senior notes is a Level 2 measurement that is determined using recent bid prices.

Index

The table below presents the fair and carrying values of the Company's convertible senior notes at April 28, 2013 and October 28, 2012.

	April 28, 2013		October 28, 2012	
	Fair Value	Carrying Value	Fair Value	Carrying Value
3.25% convertible senior notes	$125,247	$ 115,000	$110,239	$ 115,000
5.5% convertible senior notes	$35,288	$ 22,054	$27,755	$ 22,054

NOTE 14 - SUBSIDIARY SHARE REPURCHASE AND TENDER OFFER

Since the second quarter of fiscal 2011, the board of directors of PSMC, a subsidiary of the Company based in Taiwan, has authorized several share repurchase programs for PSMC to purchase for retirement shares of its outstanding common stock. The last of these repurchase programs concluded in the first quarter of fiscal 2013. During the six month period ended April 28, 2013, PSMC purchased 9.2 million shares at a cost of $4.2 million. PSMC did not purchase any shares during the three month period ended April 28, 2013. PSMC purchased 15.7 million shares at a cost of $6.7 million and 18.0 million shares at a cost of $7.6 million during the three and six month periods ended April 29, 2012, respectively. These repurchase programs increased the Company's ownership in PSMC to 66.81% at April 29, 2012, 72.09% at October 28, 2012, and 75.11% at January 27, 2013.

In April 2013 PSMC obtained approval from Taiwan's GreTai Securities Market ("GTSM") to delist its stock from the GTSM. On April 30, 2013, the Company commenced a tender offer, which is expected to conclude on June 18, 2013, to acquire the outstanding shares of PSMC that it does not currently own at NTD16.30 per share. The Company expects, upon completion of the tender offer, to acquire the tendered shares at an estimated cost of up to approximately $30 million, should substantially all of the remaining outstanding shares be tendered.

The table below presents the effect of the change in the Company’s ownership interest in PSMC on the Company's equity for the three and six month periods ended April 28, 2013 (9.2 million shares of common stock of PSMC repurchased) and April 29, 2012 (15.7 million shares and 18.0 million of PSMC stock repurchased, respectively). There were no shares of common stock of PSMC repurchased during the three month period ended April 28, 2013.

	Three Months Ended		Six Months Ended	
	April 28, 2013	April 29, 2012	April 28, 2013	April 29, 2012
Net income attributable to Photronics, Inc. shareholders	$4,863	$8,818	$7,187	$13,086
Increase in Photronics, Inc.'s additional paid-in capital	-	866	579	1,017
Decrease in accumulated other comprehensive income	-	(32)	(27)	(35)
Change from net income attributable to Photronics, Inc. shareholders and transfer from noncontrolling interest	$4,863	$9,652	$7,739	$14,068

NOTE 15 - COMMITMENTS AND CONTINGENCIES

As of April 28, 2013, the Company had commitments outstanding for capital expenditures of approximately $58 million. See Note 14 for discussion of the Company’s tender offer to acquire the outstanding shares of PSMC.

The Company is subject to various claims that arise in the ordinary course of business. The Company believes such claims, individually or in the aggregate, will not have a material effect on its condensed consolidated financial statements.

Index

NOTE 16 - RECENT ACCOUNTING PRONOUNCEMENTS

In February 2013 the Financial Accounting Standards Board issued Accounting Standards Update (ASU) No. 2013-02, “Reporting Amounts Reclassified Out of Other Comprehensive Income”. The amendments included in ASU No. 2013-02 require an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component, and present changes in accumulated balances for each component of comprehensive income on an interim basis. The Company adopted the provisions of ASU No. 2013-02 in the three month period ended April 28, 2013, as disclosed in Note 11.

Item 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Overview

Management's discussion and analysis ("MD&A") of the Company's financial condition, results of operations and outlook should be read in conjunction with its condensed consolidated financial statements and related notes. Various segments of this MD&A contain forward-looking statements, all of which are presented based on current expectations and may be adversely affected by uncertainties and risk factors (presented throughout this filing and in the Company's Annual Report on Form 10-K for the fiscal 2012 year), that may cause actual results to materially differ from these expectations.

The Company sells substantially all of its photomasks to semiconductor designers and manufacturers, and manufacturers of FPDs. Photomask technology is also being applied to the fabrication of other higher performance electronic products such as photonics, micro-electronic mechanical systems and certain nanotechnology applications. Thus, the Company's selling cycle is tightly interwoven with the development and release of new semiconductor designs and flat panel applications, particularly as it relates to the semiconductor industry's migration to more advanced design methodologies and fabrication processes. The Company believes that the demand for photomasks primarily depends on design activity rather than sales volumes from products produced using photomask technologies. Consequently, an increase in semiconductor or FPD sales does not necessarily result in a corresponding increase in photomask sales. However, the reduced use of customized ICs, reductions in design complexity, other changes in the technology or methods of manufacturing or designing semiconductors, or a slowdown in the introduction of new semiconductor or FPD designs could reduce demand for photomasks even if demand for semiconductors and FPDs increases. Advances in semiconductor, FPD and photomask design and semiconductor production methods could also reduce the demand for photomasks. Historically, the semiconductor industry has been volatile, with sharp periodic downturns and slowdowns. These downturns have been characterized by, among other things, diminished product demand, excess production capacity and accelerated erosion of selling prices.

The global semiconductor industry is driven by end markets which have been closely tied to consumer driven applications of high performance semiconductor devices including, but not limited to, mobile communications and computing solutions. The Company is typically required to fulfill its customer orders within a short period of time, sometimes within 24 hours. This results in the Company having a minimal level of backlog orders, typically one to two weeks for IC photomasks and two to three weeks for FPD photomasks. The Company cannot predict the timing of the industry's transition to volume production of next generation technology nodes or the timing of up and down cycles with precise accuracy, but believes that such transitions and cycles will continue into the future, beneficially and adversely affecting its business, financial condition and operating results in the near term. The Company believes its ability to remain successful in these environments is dependent upon achieving its goals of being a service and technology leader and efficient solutions supplier, which it believes should enable it to continually reinvest in its global infrastructure.

Index

Material Changes in Results of Operations
Three and Six Months ended April 28, 2013 and April 29, 2012

The following table represents selected operating information expressed as a percentage of net sales.

	Three Months Ended		Six Months Ended	
	April 28, 2013	April 29, 2012	April 28, 2013	April 29, 2012
Net sales	100.0 %	100.0 %	100.0 %	100.0 %
Cost of sales	(76.8)	(74.6)	(77.8)	(75.9)
Gross margin	23.2	25.4	22.2	24.1
Selling, general and administrative expenses	(11.4)	(10.4)	(11.2)	(10.2)
Research and development expenses	(4.2)	(3.8)	(4.6)	(3.9)
Consolidation, restructuring and related charges	-	-	-	(0.5)
Operating income	7.6	11.2	6.4	9.5
Other income (expense), net	(0.9)	(0.8)	(0.7)	(0.6)
Net income before income tax provision	6.7	10.4	5.7	8.9
Income tax provision	(1.6)	(2.3)	(1.7)	(2.6)
Net income	5.1	8.1	4.0	6.3
Net income attributable to noncontrolling interests	(0.5)	(0.6)	(0.5)	(0.6)
Net income attributable to Photronics, Inc. shareholders	4.6 %	7.5 %	3.5 %	5.7 %

Note: All of the following tabular comparisons, unless otherwise indicated, are for the three months ended April 28, 2013 (Q2-13) and April 29, 2012 (Q2-12) and for the six months ended April 28, 2013 (YTD-13) and April 29, 2012 (YTD-12), in millions of dollars.

Net Sales

	Three Months Ended			Six Months Ended		
	Q2-13	Q2-12	Percent Change	YTD-13	YTD-12	Percent Change
IC	$82.2	$89.1	(7.8)%	$156.6	$175.9	(11.0)%
FPD	24.5	28.4	(13.5)%	49.9	53.7	(7.0)%
Total net sales	$106.7	$117.5	(9.2)%	$206.5	$229.6	(10.1)%

Net sales for Q2-13 decreased 9.2% to $106.7 million as compared to $117.5 million for Q2-12. The decrease was primarily a result of general softness within the semiconductor industry compared to Q2-12. Revenues attributable to high-end products decreased by $10.7 million to $39.9 million in Q2-13 as compared to $50.6 million in Q2-12. High-end photomask applications include mask sets for 45 nanometer and below for IC products, and G8 and above and active matrix organic light-emitting diode (AMOLED) display screen technologies for FPD products. By geographic area, net sales in Q2-13 as compared to Q2-12 decreased by $9.2 million or 22.1% in Korea, $0.1 million or 0.2% in the United States, $0.3 million or 0.9% in Taiwan, $1.0 million or 9.6% in Europe and $0.2 million at other international locations.

Index

Net sales for YTD-13 decreased 10.1% to $206.5 million as compared to $229.6 million for YTD-12. The decrease was primarily a result of general softness within the semiconductor industry compared to YTD-12. Revenues attributable to high-end products decreased by $18.3 million to $75.1 million in YTD-13 as compared to $93.4 million in YTD-12. The Company's quarterly revenues can be affected by the seasonal purchasing of its customers. Demand for the Company's products is typically negatively impacted during the first six months of its fiscal year by the North American, European and Asian holiday periods, as some customers reduce their effective workdays and orders during this period.

Gross Margin

	Three Months Ended			Six Months Ended		
	Q2-13	Q2-12	Percent Change	YTD-13	YTD-12	Percent Change
Gross margin	$24.8	$29.9	(17.0)%	$45.9	$55.3	(17.1)%
Percentage of net sales	23.2%	25.4%		22.2%	24.1%	

Gross margin percentage decreased to 23.2% in Q2-13 from 25.4% in Q2-12 and decreased to 22.2% in YTD-13 from 24.1% in YTD-12. These decreases were a result of decreased sales in Q2-13 as compared to Q2-12 and for the first six months of 2013 as compared to the same period in FY2012. The Company operates in a high fixed cost environment and, to the extent that the Company's revenues and utilization increase or decrease, gross margin will generally be positively or negatively impacted.

Selling, General and Administrative Expenses

	Three Months Ended			Six Months Ended		
	Q2-13	Q2-12	Percent Change	YTD-13	YTD-12	Percent Change
Selling, general and administrative expenses	$12.2	$12.2	-	$23.2	$23.5	(1.3)%
Percentage of net sales	11.4%	10.4%		11.2%	10.2%	

Selling, general and administrative expenses were $12.2 million in Q2-13 and Q2-12, and were $23.2 million in YTD-13, down slightly from $23.5 million in YTD-12 due to reduced selling-related expenses.

Research and Development

	Three Months Ended			Six Months Ended		
	Q2-13	Q2-12	Percent Change	YTD-13	YTD-12	Percent Change
Research and development	$4.6	$4.4	2.6%	$9.4	$8.9	5.7%
Percentage of net sales	4.2%	3.8%		4.6%	3.9%	

Research and development expenses consist primarily of global development efforts related to high-end process technologies for advanced sub-wavelength reticle solutions for IC technologies. Research and development expenses increased by $0.2 million to $4.6 million in Q2-13, as compared to $4.4 million in Q2-12, and by $0.5 million to $9.4 million in YTD-13, as compared to $8.9 million in YTD-12. The increase in research and development expenses in Q2-13 and YTD-13 as compared to the same periods in the prior year was primarily due to increased activities at advanced technology nodes for IC photomasks.

Index

Consolidation, Restructuring and Related Charges

	Three Months Ended		Six Months Ended	
	Q2-13	Q2-12	YTD-13	YTD-12
Employee terminations and other	$-	$28	$-	$914
Asset write-downs	-	30	-	262
Total consolidation, restructuring and related charges	$-	$58	$-	$1,176

In the first quarter of fiscal 2012 the Company ceased the manufacture of photomasks at its Singapore facility and, in connection therewith, recorded charges of $0.1 million and $1.2 million during the three and six month periods ended April 29, 2012. This restructuring, which was comprised primarily of employee termination costs, was substantially completed in fiscal 2012 at a total cost of $1.4 million.

Other Income (Expense), net

	Three Months Ended		Six Months Ended	
	Q2-13	Q2-12	YTD-13	YTD-12
Interest expense	$(1.9)	$(1.8)	$(3.8)	$(3.6)
Interest and other income (expense), net	1.0	0.8	2.3	2.2
Other income (expense), net	$(0.9)	$(1.0)	$(1.5)	$(1.4)

Interest expense increased slightly in Q2-13 as compared to Q2-12 and in YTD-13 as compared to YTD-12, primarily as a result of the term loan entered into in the second quarter of fiscal year 2012.

Interest and other income (expense), net increased in Q2-13 as compared to Q2-12 by $0.2 million, and in YTD-13 as compared to YTD-12 by $0.1 million as a result of higher foreign currency exchange gains.

Income Tax Provision

	Three Months Ended		Six Months Ended	
	Q2-13	Q2-12	YTD-13	YTD-12
Income tax provision	$1.7	$2.7	$3.5	$6.0
Effective income tax rate	24.1 %	21.8 %	29.5 %	29.4 %

The effective income tax rate increased in Q2-13 as compared to Q2-12, and in YTD-13 as compared to YTD-12, primarily due to higher income tax provisions recorded in jurisdictions in which the Company generated income before income taxes which, due to valuation allowances, were not significantly offset by income tax benefits recorded in jurisdictions in which the Company incurred losses before income taxes.

Net Income Attributable to Noncontrolling Interests

Net income attributable to noncontrolling interests decreased $0.1 million to $0.6 million in Q2-13, as compared to $0.7 million in Q2-12, and $0.2 million to $1.1 million in YTD-13 , as compared to $1.3 million in YTD-12, primarily as a result of share repurchase programs at PSMC, the Company's non-wholly owned subsidiary in Taiwan. As a result of these programs, the Company’s ownership percentage in PSMC at the end of Q2-13 had increased to 75.11%

from 66.81% at the end of Q2-12. The Company’s ownership percentage in its subsidiary in Korea was 99.7% in Q2-13 and Q2-12.

Index

Liquidity and Capital Resources

The Company's working capital was $207.0 million at April 28, 2013, and $234.3 million at October 28, 2012. The decrease in working capital was primarily the result of increased accounts payable related to capital equipment. Cash and cash equivalents were approximately $211 million at April 28, 2013 and $218 million at October 28, 2012. The decrease in cash and cash equivalents was primarily the result of capital expenditure payments. Net cash provided by operating activities was $35.9 million for the six month period ended April 28, 2013, a decrease from $62.4 million for the six month period ended April 29, 2012, primarily as a result of decreased net income and increased accounts receivable and inventory balances during the period. Net cash used in investing activities for the six month period ended April 28, 2013, was $34.7 million, which was comprised primarily of capital expenditure payments. Net cash used in financing activities of $7.0 million for the six month period ended April 28, 2013, was primarily comprised of payments to repurchase the common stock of a subsidiary and repayments of long-term borrowings. The Company may use its cash available on hand for operations, capital expenditures, debt repayments, strategic opportunities, stock repurchases or other corporate uses, any of which may be material.

The Company's credit facility bears interest (2.5% at April 28, 2013), based on the Company's total leverage ratio, at LIBOR plus a spread, as defined in the credit facility. The credit facility is secured by substantially all of the Company's assets located in the United States, as well as common stock the Company owns in certain of its foreign subsidiaries, and is subject to the following financial covenants: minimum fixed charge ratio, total leverage ratio and minimum unrestricted cash balance. As of April 28, 2013, the Company was in compliance with the covenants of its credit facility, had no outstanding borrowings under the credit facility and $30 million was available for borrowing.

In February 2013 the Company entered into a five year capital lease to fund the purchase of a high-end lithography tool. The principal amount of the lease, which is currently estimated to be approximately $27 million, will be determined by the Japanese yen exchange rate to the U.S. dollar as progress payments are made on the tool. The interest rate will be fixed, based on the five year interest rate swap plus a spread, upon acceptance of the tool which is expected to occur in the fourth quarter of fiscal year 2013. Progress payments totaling $6.9 million have been made by the lessor through April 28, 2013, and are included in the Company's long-term borrowings amount as of that date.

Since the second quarter of fiscal 2011, the board of directors of PSMC, a subsidiary of the Company based in Taiwan, has authorized several share repurchase programs for PSMC to purchase for retirement shares of its outstanding common stock. The last of these repurchase programs concluded in the first quarter of fiscal 2013. During the six month period ended April 28, 2013, PSMC purchased 9.2 million shares at a cost of $4.2 million. PSMC did not purchase any shares during the three month period ended April 28, 2013. PSMC purchased 15.7 million shares at a cost of $6.7 million and 18.0 million shares at a cost of $7.6 million during the three and six month periods ended April 29, 2012, respectively. These repurchase programs increased the Company's ownership in PSMC to 66.81% at April 29, 2012, 72.09% at October 28, 2012, and 75.11% at January 27, 2013.

In April 2013 PSMC obtained approval from Taiwan's GreTai Securities Market ("GTSM") to delist its stock from the GTSM. On April 30, 2013, the Company commenced a tender offer, which is expected to conclude on June 18, 2013, to acquire the outstanding shares of PSMC that it does not currently own at NTD16.30 per share. The Company expects, upon completion of the tender offer, to acquire the tendered shares at an estimated cost of up to approximately $30 million, should substantially all of the remaining outstanding shares be tendered.

At April 28, 2013, the Company had capital commitments outstanding of approximately $58 million. The Company believes that its currently available resources, together with its capacity for growth, and its access to equity and other financing sources, will be sufficient to satisfy its currently planned capital expenditures, as well as its anticipated working capital requirements for the next twelve months. However, the Company cannot assure that additional sources of financing would be available to the Company on commercially favorable terms, should the Company's capital requirements exceed cash available from operations, existing cash, and cash available under its credit facility.

The Company's liquidity is highly dependent on its sales volume, cash conversion cycle, and the timing of its capital expenditures (which can vary significantly from period to period), as it operates in a high fixed cost environment. Depending on conditions in the semiconductor and FPD markets, the Company's cash flows from operations and current holdings of cash may not be adequate to meet its current and long-term needs for capital expenditures, operations and debt repayments. Historically, in certain years, the Company has used external financing to fund these needs. Due to conditions in the credit markets, some financing instruments used by the Company in the past may not be currently available to it. The Company continues to evaluate further cost reduction initiatives. However, the Company cannot assure that additional sources of financing would be available to it on commercially favorable terms, should its cash requirements exceed cash available from operations, existing cash, and cash available under its credit facility.

Index

Off-Balance Sheet Arrangements

Under the MP Mask joint venture operating agreement, in order to maintain its 49.99% ownership interest, the Company may be required to make additional capital contributions to the joint venture up to the maximum amount specified in the operating agreement. Cumulatively through April 28, 2013, the Company has made additional contributions of $32.5 million to the joint venture, and has received distributions from the joint venture totaling $10.0 million.

The Company leases certain office facilities and equipment under operating leases that may require it to pay taxes, insurance and maintenance expenses related to the properties. Certain of these leases contain renewal or purchase options exercisable at the end of the lease terms.

Business Outlook

A majority of the Company's revenue growth is expected to continue to come from the Asian region, as customers increase their use of manufacturing foundries located outside of North America and Europe. Additional revenue growth is also anticipated in North America, as the Company benefits from advanced technology it may utilize under its technology license with Micron. The Company's Korean and Taiwanese operations are non-wholly owned subsidiaries and, therefore, a portion of earnings generated at each of these locations is allocated to noncontrolling interests.

Ongoing Business Assessments

The Company continues to assess its global manufacturing strategy and monitor its market capitalization, sales volume and cash flows from operations. This ongoing assessment could result in future facility closures, asset redeployments, impairments of intangible or long-lived assets, workforce reductions, or the addition of increased manufacturing facilities as well as acquisitions, divestitures and joint ventures, any of which could be material. The undertaking of such transactions would be based on business and capital market conditions, financial impact, customer requirements, and business opportunities and needs, regulatory conditions and other relevant factors.

Effect of Recent Accounting Pronouncements

See Note 16 to the condensed consolidated financial statements for discussion of ASU No. 2013-02 adopted by the Company in the three month period ended April 28, 2013. There have been no other recent accounting pronouncements whose adoption would affect the Company’s condensed consolidated financial statements or related disclosures.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

Foreign Currency Exchange Rate Risk

The Company conducts business in several major international currencies through its worldwide operations and its financial position, financial performance and cash flows may be affected by fluctuations in the exchange rates of these currencies. Changes in exchange rates can positively or negatively affect the Company's sales, operating margins, assets, liabilities, and equity. The functional currencies of the Company's Asian subsidiaries are the Korean won, the New Taiwan dollar, and the Singapore dollar. The functional currencies of the Company's European subsidiaries are the British pound and the euro.

The Company attempts to minimize its risk of foreign currency transaction losses by producing its products in the same country in which the products are sold (thereby generating revenues and incurring expenses in the same currency), and by managing its working capital. In some instances, the Company may sell or purchase products in a currency other than the functional currency of the country where it was produced. There can be no assurance that this approach will continue to be successful, especially in the event of a significant adverse movement in the value of any foreign currencies against the U.S. dollar.

The Company's primary net foreign currency exposures as of April 28, 2013, included the Korean won, the Japanese yen, the New Taiwan dollar, the Singapore dollar, the British pound, and the euro. As of April 28, 2013, a 10% adverse movement in the value of these currencies against the U.S. dollar would have resulted in a net unrealized pre-tax loss of $2.0 million. The Company does not believe that a 10% change in the exchange rates of other non-U.S. dollar currencies would have a material effect on its consolidated financial position, results of operations, or cash flows.

Index

Interest Rate Risk

At April 28, 2013, the Company had $22.5 million in variable rate borrowings. A 10% change in interest rates would not have had a material effect on the Company's consolidated financial position, results of operations, or cash flows in the three and six month periods ended April 28, 2013.

Item 4. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

The Company has established and currently maintains disclosure controls and procedures, as such term is defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), designed to ensure that information required to be disclosed in its reports filed under the Exchange Act, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms, and that such information is accumulated and communicated to management, including the Company's chief executive officer and chief financial officer, as appropriate, to allow for timely decisions regarding required disclosure. In designing and evaluating disclosure controls and procedures, management recognized that any controls and procedures, no matter how well designed and operated, can provide only reasonable assurance of achieving the desired control objectives, and management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible controls and procedures.

The Company's management, under the supervision and with the participation of the Company’s chief executive officer and chief financial officer, evaluated the effectiveness of the design and operation of the Company’s disclosure controls and procedures as of the end of the period covered by this report. Based upon that evaluation the Company’s chief executive officer and chief financial officer concluded that the Company’s disclosure controls and procedures were effective at a reasonable assurance level as of the end of the period covered by this report.

Changes in Internal Control over Financial Reporting

There was no change in the Company's internal control over financial reporting during the Company's second quarter of fiscal 2013 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 to risks relating to the Company's business as disclosed in Part 1, Item 1A of the Company's Form 10-K for the year ended October 28, 2012.

Index

Item 6. EXHIBITS

(a) Exhibits

Exhibit Number	Description
31.1	Certification of Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Securities Exchange Act of 1934, as adopted 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 Financial Officer 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 Extension Calculation Linkbase Document
101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	XBRL Taxonomy Extension Label Linkbase Document
101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

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.

Photronics, Inc.
(Registrant)

By: /s/ SEAN T. SMITH
Sean T. Smith
Senior Vice President

Chief Financial Officer
(Duly Authorized Officer
and Principal Financial
Officer)

Date: June 5, 2013