

TRANSACT TECHNOLOGIES INC
Form 10-Q
August 07, 2013

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended: June 30, 2013
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: 0-21121

(Exact name of registrant as specified in its charter)

Delaware 06-1456680
(State or Other Jurisdiction of Incorporation or (I.R.S. Employer Identification No.)
Organization)

One Hamden Center, 2319 Whitney Avenue, Suite 3B,
Hamden, CT 06518
(Address of Principal Executive Offices) (Zip Code)

(203) 859-6800
(Registrant's Telephone Number, Including
Area Code)

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

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

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 No

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

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) Smaller reporting company

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

As of July 31, 2013, the number of shares outstanding of the Company’s common stock, \$0.01 par value, was 8,691,205.

TRANSACT TECHNOLOGIES INCORPORATED

INDEX

| <u>PART I - Financial Information:</u> | | Page |
|--|--|------|
| Item 1 | <u>Financial Statements (unaudited)</u> | |
| | <u>Condensed Consolidated Balance Sheets as of June 30, 2013 and December 31, 2012</u> | 3 |
| | <u>Condensed Consolidated Statements of Income for the three and six months ended June 30, 2013 and 2012</u> | 4 |
| | <u>Condensed Consolidated Statements of Comprehensive Income for the three and six months ended June 30, 2013 and 2012</u> | 5 |
| | <u>Condensed Consolidated Statements of Cash Flows for the six months ended June 30, 2013 and 2012</u> | 6 |
| | <u>Notes to Condensed Consolidated Financial Statements</u> | 7 |
| Item 2 | <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u> | 10 |
| Item 3 | <u>Quantitative and Qualitative Disclosures About Market Risk</u> | 20 |
| Item 4 | <u>Controls and Procedures</u> | 21 |
| <u>PART II - Other Information:</u> | | |
| Item 1 | <u>Legal Proceedings</u> | 21 |
| Item 1A | <u>Risk Factors</u> | 21 |
| Item 2 | <u>Unregistered Sales of Equity Securities and Use of Proceeds</u> | 21 |
| Item 3 | <u>Defaults Upon Senior Securities</u> | 21 |
| Item 4 | <u>Mine Safety Disclosures</u> | 21 |
| Item 5 | <u>Other Information</u> | 21 |
| Item 6 | <u>Exhibits</u> | 22 |
| | <u>SIGNATURES</u> | 23 |

PART I - FINANCIAL INFORMATION

Item 1. FINANCIAL STATEMENTS

TRANSACT TECHNOLOGIES INCORPORATED
CONDENSED CONSOLIDATED BALANCE SHEETS
(unaudited)

| | June 30, 2013 | December 31, 2012 |
|---|-----------------------------------|-------------------------|
| | (In thousands, except share data) | |
| Assets: | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 8,828 | \$ 7,537 |
| Accounts receivable, net | 11,640 | 15,927 |
| Inventories | 12,787 | 10,321 |
| Deferred tax assets | 1,443 | 1,443 |
| Other current assets | 666 | 471 |
| Total current assets | 35,364 | 35,699 |
| Fixed assets, net | 3,105 | 3,302 |
| Goodwill | 2,621 | 2,621 |
| Deferred tax assets | 1,113 | 1,172 |
| Intangible assets, net of accumulated amortization of \$1,554 and \$1,298, respectively | 2,113 | 2,328 |
| Other assets | 79 | 106 |
| | 9,031 | 9,529 |
| Total assets | \$ 44,395 | \$ 45,228 |
| Liabilities and Shareholders' Equity: | | |
| Current liabilities: | | |
| Accounts payable | \$ 5,603 | \$ 6,422 |
| Accrued liabilities | 2,391 | 2,927 |
| Income taxes payable | 121 | 629 |
| Accrued contingent consideration (Note 4) | 230 | 136 |
| Deferred revenue | 197 | 93 |
| Total current liabilities | 8,542 | 10,207 |
| Deferred revenue, net of current portion | 166 | 168 |
| Deferred rent, net of current portion | 278 | 308 |
| Accrued contingent consideration, net of current portion (Note 4) | 530 | 824 |
| Other liabilities | 383 | 352 |
| | 1,357 | 1,652 |
| Total liabilities | 9,899 | 11,859 |
| Shareholders' equity: | | |
| | 110 | 109 |

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| | | |
|--|-----------|-----------|
| Common stock, \$0.01 par value, 20,000,000 shares authorized; 10,988,080 and 10,903,077 shares issued, respectively; 8,691,205 and 8,720,200 shares outstanding, respectively | | |
| Additional paid-in capital | 26,732 | 25,940 |
| Retained earnings | 25,956 | 24,708 |
| Accumulated other comprehensive loss, net of tax | (82) | (55) |
| Treasury stock, at cost, 2,297,038 and 2,182,877 shares, respectively | (18,220) | (17,333) |
| Total shareholders' equity | 34,496 | 33,369 |
| Total liabilities and shareholders' equity | \$ 44,395 | \$ 45,228 |

See notes to Condensed Consolidated Financial Statements.

TRANSACT TECHNOLOGIES INCORPORATED
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
(unaudited)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|---|---------------------------------------|-----------|------------------------------|-----------|
| | 2013 | 2012 | 2013 | 2012 |
| | (In thousands, except per share data) | | | |
| Net sales | \$ 15,788 | \$ 15,853 | \$ 30,845 | \$ 33,412 |
| Cost of sales | 9,336 | 10,011 | 17,960 | 20,792 |
| Gross profit | 6,452 | 5,842 | 12,885 | 12,620 |
| Operating expenses: | | | | |
| Engineering, design and product development | 995 | 952 | 2,007 | 2,165 |
| Selling and marketing | 1,857 | 1,674 | 3,643 | 3,275 |
| General and administrative | 1,736 | 1,903 | 3,770 | 3,903 |
| Legal fees associated with lawsuit (Note 9) | 57 | 471 | 256 | 471 |
| Business consolidation and restructuring (Note 8) | - | 63 | - | 117 |
| | 4,645 | 5,063 | 9,676 | 9,931 |
| Operating income | 1,807 | 779 | 3,209 | 2,689 |
| Interest and other income (expense): | | | | |
| Interest, net | - | 2 | (1) | 4 |
| Other, net | (4) | 13 | 33 | (11) |
| | (4) | 15 | 32 | (7) |
| Income before income taxes | 1,803 | 794 | 3,241 | 2,682 |
| Income tax provision | 588 | 286 | 866 | 966 |
| Net income | \$ 1,215 | \$ 508 | \$ 2,375 | \$ 1,716 |
| Net income per common share: | | | | |
| Basic | \$ 0.14 | \$ 0.06 | \$ 0.27 | \$ 0.19 |
| Diluted | \$ 0.14 | \$ 0.06 | \$ 0.27 | \$ 0.18 |
| Shares used in per-share calculation: | | | | |
| Basic | 8,728 | 9,084 | 8,722 | 9,256 |
| Diluted | 8,802 | 9,189 | 8,803 | 9,357 |
| Dividends declared and paid per common share: | \$ 0.07 | \$ - | \$ 0.13 | \$ - |

See notes to Condensed Consolidated Financial Statements.

TRANSACT TECHNOLOGIES INCORPORATED
 CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
 (unaudited)

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|--------------------------------|--------|------------------------------|----------|
| | 2013 | 2012 | 2013 | 2012 |
| | (In thousands) | | | |
| Net income | \$ 1,215 | \$ 508 | \$ 2,375 | \$ 1,716 |
| Foreign currency translation adjustment, net of tax | 1 | (8) | (27) | 3 |
| Comprehensive income | \$ 1,216 | \$ 500 | \$ 2,348 | \$ 1,719 |

See notes to Condensed Consolidated Financial Statements.

TRANSACT TECHNOLOGIES INCORPORATED
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

| | Six Months Ended June 30, | |
|--|------------------------------|----------|
| | 2013 | 2012 |
| | (In thousands) | |
| Cash flows from operating activities: | | |
| Net income | \$ 2,375 | \$ 1,716 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Share-based compensation expense | 276 | 284 |
| Incremental tax benefits from stock options exercised | (33) | (42) |
| Depreciation and amortization | 886 | 885 |
| Loss on sale of fixed assets | - | 2 |
| Foreign currency transaction (gains) losses | (33) | 8 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable | 4,277 | (2,072) |
| Inventories | (2,467) | 2,500 |
| Prepaid income taxes | - | 161 |
| Other current and long term assets | (166) | (204) |
| Accounts payable | (818) | 1,853 |
| Accrued liabilities and other liabilities | (990) | 580 |
| Net cash provided by operating activities | 3,307 | 5,671 |
| Cash flows from investing activities: | | |
| Capital expenditures | (426) | (339) |
| Additions to capitalized software | (42) | (10) |
| Net cash used in investing activities | (468) | (349) |
| Cash flows from financing activities: | | |
| Proceeds from stock option exercises | 446 | 145 |
| Payment of dividends on common stock | (1,127) | - |
| Purchases of common stock for treasury | (887) | (5,151) |
| Incremental tax benefits from stock options exercised | 33 | 42 |
| Net cash used in financing activities | (1,535) | (4,964) |
| Effect of exchange rate changes on cash and cash equivalents | (13) | (9) |
| Increase in cash and cash equivalents | 1,291 | 349 |
| Cash and cash equivalents, beginning of period | 7,537 | 6,863 |
| Cash and cash equivalents, end of period | \$ 8,828 | \$ 7,212 |

See notes to Condensed Consolidated Financial Statements.

TRANSACT TECHNOLOGIES INCORPORATED
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

1. Basis of presentation

The accompanying unaudited financial statements of TransAct Technologies Incorporated have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information. Accordingly, they do not include all of the information and footnotes required by accounting principles generally accepted in the United States of America to be included in full year financial statements. In the opinion of management, all adjustments considered necessary for a fair statement of the results for the periods presented have been included and are of a normal recurring nature. The December 31, 2012 Condensed Consolidated Balance Sheet data was derived from audited financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America. These interim financial statements should be read in conjunction with the audited financial statements for the year ended December 31, 2012 included in our Annual Report on Form 10-K.

The financial position and results of operations of our U.K. foreign subsidiary are measured using local currency as the functional currency. Assets and liabilities of such subsidiary have been translated at the end of period exchange rates, and related revenues and expenses have been translated at the weighted average exchange rates with the resulting translation gain or loss recorded in accumulated other comprehensive income (loss) in the Condensed Consolidated Balance Sheets. Transaction gains and losses are included in other income in the Condensed Consolidated Statements of Income.

The results of operations for the three and six months ended June 30, 2013 are not necessarily indicative of the results to be expected for the full year.

2. Inventories

The components of inventories are:

| | June 30, 2013 | December 31, 2012 |
|---|------------------|-------------------------|
| (In thousands) | | |
| Raw materials and purchased component parts | \$ 9,055 | \$ 6,871 |
| Finished goods | 3,732 | 3,450 |
| | \$ 12,787 | \$ 10,321 |

3. Accrued product warranty liability

We generally warrant our products for up to 36 months and record the estimated cost of such product warranties at the time the sale is recorded. Estimated warranty costs are based upon actual past experience of product repairs and the related estimated cost of labor and material to make the necessary repairs.

The following table summarizes the activity recorded in the accrued product warranty liability during the six months ended June 30, 2013:

| | (In thousands) |
|--|-------------------|
| Balance, beginning of period | \$ 274 |
| Accruals for warranties issued during the period | 46 |
| Changes in estimates | 194 |
| Settlements during the period | (172) |
| Balance, end of period | \$ 342 |

Approximately \$90,000 of the accrued product warranty liability is classified as a long-term liability, in Other liabilities, at June 30, 2013 in the Condensed Consolidated Balance Sheets.

7

TRANSACT TECHNOLOGIES INCORPORATED
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

4. Accrued contingent consideration

In connection with the acquisition of substantially all of the assets of Printrex, Inc. ("Printrex") on August 19, 2011, we entered into a contingent consideration arrangement for 30% of the gross profit for a three-year period related to certain new products under development, less certain other adjustments, beginning on the earlier of 1) January 1, 2012 or 2) the date of first commercial introduction of the new products under development. The undiscounted fair value related to the contingent liability could range from approximately \$200,000 to \$1,600,000. The fair value of the contingent consideration arrangement was \$760,000 and \$960,000 at June 30, 2013 and December 31, 2012, respectively, which was estimated by applying the income approach. That measure is based on significant inputs that are not observable in the market, which fair value measurement guidance refers to as Level 3 inputs. During the second quarter of 2013, the fair value of the contingent consideration decreased by \$200,000 and this credit is included in general and administrative expenses on the Condensed Consolidated Statements of Income. No payments were made under the arrangement during the six months ended June 30, 2013 as the underlying conditions of the contingent consideration arrangement were not satisfied. Refer to Note 3, Business acquisitions, to the Company's Consolidated Financial Statements included in the Company's 2012 Annual Report on Form 10-K for the year ended December 31, 2012 for additional information regarding this contingent consideration arrangement.

5. Earnings per share

The following table sets forth the reconciliation of basic weighted average shares outstanding and diluted weighted average shares outstanding:

| | Three Months Ended June 30, | | Six Months Ended June 30, | |
|--|---------------------------------------|---------|------------------------------|----------|
| | 2013 | 2012 | 2013 | 2012 |
| | (In thousands, except per share data) | | | |
| Net income | \$ 1,215 | \$ 508 | \$ 2,375 | \$ 1,716 |
| Shares: | | | | |
| Basic: Weighted average common shares outstanding | 8,728 | 9,084 | 8,722 | 9,256 |
| Add: Dilutive effect of outstanding options as determined by the treasury stock method | 74 | 105 | 81 | 101 |
| Diluted: Weighted average common and common equivalent shares outstanding | 8,802 | 9,189 | 8,803 | 9,357 |
| Net income per common share: | | | | |
| Basic | \$ 0.14 | \$ 0.06 | \$ 0.27 | \$ 0.19 |
| Diluted | \$ 0.14 | \$ 0.06 | \$ 0.27 | \$ 0.18 |

For the three months ended June 30, 2013 and 2012, there were 565,000 and 507,125, respectively, potentially dilutive shares consisting of stock options that were excluded from the calculation of earnings per diluted share. For the six months ended June 30, 2013 and 2012, there were 636,000 and 585,125, respectively, potentially dilutive shares consisting of stock options that were excluded from the calculation of earnings per diluted share.

6. Shareholders' equity

Changes in shareholders' equity for the six months ended June 30, 2013 were as follows (in thousands):

| | |
|---|----------|
| Balance at December 31, 2012 | \$33,369 |
| Net income | 2,375 |
| Proceeds from issuance of shares from exercise of stock options | 446 |
| Share-based compensation expense | 276 |
| Issuance of deferred stock units, net of relinquishments | 111 |
| Incremental tax benefits from stock options exercised | 33 |
| Foreign currency translation adjustment | (27) |
| Reversal of deferred tax asset in connection with stock options forfeited | (73) |
| Purchases of common stock for treasury | (887) |
| Dividends declared and paid on common stock | (1,127) |
| Balance at June 30, 2013 | \$34,496 |

We paid a portion of the 2012 incentive bonus for the chief executive officer and chief financial officer in the form of deferred stock units. Such deferred stock units were granted in March 2013 and were fully vested at the time of grant.

For the three months ended June 30, 2013, our Board of Directors declared a quarterly cash dividend of \$0.07 per share, totaling approximately \$608,000, which was paid in June 2013 to common shareholders of record at the close of business on May 20, 2013. For the six months ended June 30, 2013, dividends declared and paid totaled \$1,127,000, or \$0.13 per share.

TRANSACT TECHNOLOGIES INCORPORATED
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(unaudited)

7. Income taxes

We recorded an income tax provision for the second quarter of 2013 of \$588,000 at an effective tax rate of 32.6%, compared to an income tax provision during the second quarter of 2012 of \$286,000 at an effective tax rate of 36.0%. For the six months ended June 30, 2013, we recorded an income tax provision of \$866,000 at an effective tax rate of 26.7%, compared to an income tax provision during the six months ended June 30, 2012 of \$966,000 at an effective tax rate of 36.0%. Our effective tax rate for the second quarter of 2013 is lower than the second quarter of 2012 primarily because it includes the benefit from the federal research and development credit which was not included in the 2012 income tax provision since it expired at the end of 2011. Our effective tax rate for the first six months of 2013 is unusually low because it includes the benefit from the 2012 federal research and development (“R&D”) credit of approximately \$220,000 as this credit was not renewed until January 2, 2013 as a component of the American Taxpayer Relief Act of 2012 (the “Act”). The effective tax rate for the first six months of 2013 was also favorably impacted by the benefit from the 2013 R&D credit.

We are subject to U.S. federal income tax as well as income tax of certain state and foreign jurisdictions. We have substantially concluded all U.S. federal income tax, state and local, and foreign tax matters through 2003. During 2008, a limited scope examination of our 2005 and 2006 federal tax returns was completed. However, our federal tax returns for the years 2004 through 2011 remain open to examination and as of June 30, 2013, our 2010 federal tax return is under examination. Various state and foreign tax jurisdiction tax years remain open to examination as well, though we believe that any additional assessment would be immaterial to the Condensed Consolidated Financial Statements. No state or foreign tax jurisdiction income tax returns are currently under examination. As of June 30, 2013, we had \$293,000 of total gross unrecognized tax benefits that, if recognized, would favorably affect the effective income tax rate in any future periods.

8. Business consolidation and restructuring expenses

As discussed in Note 8, Accrued business consolidation and restructuring expenses, to the Company’s Consolidated Financial Statements included in the Company’s 2012 Annual Report on Form 10-K for the year ended December 31, 2012, in January 2012, we determined that we no longer needed to maintain the existing Printrex manufacturing facility in San Jose, California, along with certain redundant headcount. As a result, we incurred expenses of \$63,000 and \$117,000, respectively, in the first three and six months of 2012 for employee termination benefits related to these employee reductions as well as moving costs related to the closing of the San Jose manufacturing operations. This restructuring charge was recorded in accordance with ASC 420-10-25-4 “Exit or Disposal Cost Obligations” and cash payments made under this restructuring plan were completed by October 2012.

9. Commitments and contingencies

On June 8, 2012, Avery Dennison Corporation (“AD”) filed a civil complaint against the Company and a former employee of the Company and of AD, in the Court of Common Pleas (the “Court”) in Lake County, Ohio. The complaint alleges that this former employee and the Company misappropriated unspecified trade secrets and confidential information related to the design of our food safety terminals from AD. The complaint requests a preliminary and permanent injunction against the Company from manufacturing and selling our Ithaca® 9700 and

9800 food safety terminals. On July 16, 2012, the Company filed its answer, affirmative defenses and counterclaims, seeking all available damages including legal fees. A hearing on the plaintiff's motion for preliminary injunction took place in August 2012, and in November 2012, the Court denied this request. AD filed an appeal of the Court's ruling to the Eleventh Appellate District, which heard oral arguments on the appeal on July 16, 2013. On July 23, 2013, AD requested that the Eleventh Appellate District enjoin the Company's further sale and marketing of the food safety terminals, pending the appeals court's decision. On July 29, 2013, TransAct opposed this request. The rulings by the Eleventh District of Appeals on both the appeal and request are pending.

9

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Forward Looking Statements

Certain statements included in this report, including without limitation statements in this Management's Discussion and Analysis of Financial Condition and Results of Operations, which are not historical facts are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. Forward-looking statements generally can be identified by the use of forward-looking terminology, such as "may", "will", "expect", "intend", "estimate", "anticipate", "believe", "project" or "contingent" and other similar words. All forward-looking statements involve risks and uncertainties, including, but not limited to those listed in Item 1A of our most recently filed Annual Report on Form 10-K. Actual results may differ materially from those discussed in, or implied by, the forward-looking statements. The forward-looking statements speak only as of the date of this report and we assume no duty to update them.

Overview

TransAct Technologies Incorporated ("TransAct") designs, develops and sells market-specific solutions, including printers, terminals, software and other products for transaction-based and other industries. These world-class products are sold under the Epic, EPICENTRAL™, Ithaca® and Printrex® brand names. Known and respected worldwide for innovative designs and real-world service reliability, our thermal, inkjet and impact printers and terminals generate top-quality labels and transaction records such as receipts, tickets, coupons, register journals and other documents as well as printed logging and plotting of data. We focus on the following core markets: food safety, banking and point-of-sale ("POS"), casino and gaming, lottery, oil and gas and medical and mobile. We sell our products to original equipment manufacturers ("OEMs"), value-added resellers ("VARs"), selected distributors, as well as directly to end-users. Our product distribution spans across the Americas, Europe, the Middle East, Africa, Asia, Australia, the Caribbean Islands and the South Pacific. TransAct also provides world-class printer service, spare parts, accessories and printing supplies to its growing worldwide installed base of printers. Through our TransAct Services Group ("TSG") we provide a complete range of supplies and consumables used in the printing and scanning activities of customers in the hospitality, banking, retail, casino and gaming, government and oil and gas exploration markets. Through our webstore, www.transactsupplies.com, and our direct selling team, we address the on-line demand for these products. We operate in one reportable segment: the design, development, assembly and marketing of transaction printers and terminals and providing printer-related services, supplies and spare parts.

Critical Accounting Judgments and Estimates

Our discussion and analysis of our financial condition and results of operations are based upon our Condensed Consolidated Financial Statements, which have been prepared by us in accordance with accounting principles generally accepted in the United States of America. The presentation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenue and expenses, and disclosure of contingent assets and liabilities. Our estimates include those related to revenue recognition, inventory obsolescence, the valuation of deferred tax assets and liabilities, depreciable lives of equipment, warranty obligations, and contingent liabilities. We base our estimates on historical experience and on various other assumptions that we believe to be reasonable under the circumstances.

For a complete description of our accounting policies, see Item 7 - Management's Discussion and Analysis of Financial Condition and Results of Operations, "Critical Accounting Policies and Estimates," included in our Annual Report on Form 10-K for the year ended December 31, 2012. We have reviewed those policies and determined that they remain our critical accounting policies for the six months ended June 30, 2013.

Results of Operations: Three months ended June 30, 2013 compared to three months ended June 30, 2012

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Net Sales. Net sales, which include printer, terminal and software sales as well as sales of replacement parts, consumables and maintenance and repair services, by market for the three months ended June 30, 2013 and 2012 were as follows (in thousands, except percentages):

| | Three months ended | | Three months ended | | Change | |
|---------------------------------|--------------------|--------|--------------------|--------|----------|---------|
| | June 30, 2013 | | June 30, 2012 | | \$ | % |
| Food safety, banking and POS | \$ 3,453 | 21.9% | \$ 2,676 | 16.9% | \$ 777 | 29.0% |
| Casino and gaming | 7,322 | 46.4% | 7,112 | 44.9% | 210 | 3.0% |
| Lottery | 499 | 3.2% | 1,728 | 10.9% | (1,229) | (71.1%) |
| Printrex | 1,050 | 6.6% | 1,174 | 7.4% | (124) | (10.6%) |
| TSG | 3,464 | 21.9% | 3,163 | 19.9% | 301 | 9.5% |
| | \$ 15,788 | 100.0% | \$ 15,853 | 100.0% | \$ (65) | (0.4%) |
| International * | \$ 4,052 | 25.7% | \$ 4,258 | 26.9% | \$ (206) | (4.8%) |

*International sales do not include sales of printers made to domestic distributors or other domestic customers who may in turn ship those printers to international destinations.

Net sales for the second quarter of 2013 were relatively consistent with the same period in 2012. Printer sales volume decreased 16% to approximately 38,000 units driven primarily by a 71% decrease in unit volume from the lottery market and, to a lesser extent, a 14% decrease in unit volume from the food safety, banking and POS market. The average selling price of our printers increased approximately 14% in the second quarter of 2013 compared to the second quarter of 2012 primarily due to higher sales contributions of our Ithaca® 9700 food safety terminal. Overall, international sales decreased \$206,000, or 5%, primarily driven by lower international lottery printer sales.

Food safety, banking and POS:

Revenue from the food safety, banking and POS market includes sales of food safety terminals, hardware devices that consist of a touchscreen and one or two thermal print mechanisms, that print easy-to-read expiration and "enjoy by" date labels to help restaurants effectively manage food spoilage. Revenue from this market also includes sales of inkjet, thermal and impact printers used primarily by retailers in the restaurant (including fine dining, casual dining and fast food), hospitality, and specialty retail industries to print receipts for consumers, validate checks, or print on linerless labels or other inserted media. In addition, revenue includes sales of printers used by banks, credit unions and other financial institutions to print and/or validate receipts at bank teller stations. A summary of sales of our worldwide food safety, banking and POS products for the three months ended June 30, 2013 and 2012 is as follows (in thousands, except percentages):

| | Three months ended June 30, 2013 | | Three months ended June 30, 2012 | | Change | |
|---------------|-------------------------------------|--------|-------------------------------------|--------|--------|---------|
| | \$ | % | \$ | % | \$ | % |
| Domestic | \$ 3,344 | 96.8% | \$ 2,505 | 93.6% | \$ 839 | 33.5% |
| International | 109 | 3.2% | 171 | 6.4% | (62) | (36.3%) |
| | \$ 3,453 | 100.0% | \$ 2,676 | 100.0% | \$ 777 | 29.0% |

The increase in domestic food safety, banking and POS product revenue from the second quarter of 2012 was primarily driven by sales from our new Ithaca® 9700 food safety terminal during the quarter. This was partially offset by lower sales of our banking printers mainly due to the shipment of a large order for our Ithaca® 280 thermal receipt printer to a banking customer in the second quarter of 2012 that did not repeat in the second quarter of 2013. In addition, we experienced lower sales of our legacy POS printers as we continue to decrease our focus on this commoditized market.

Casino and gaming:

Revenue from the casino and gaming market includes sales of printers used in slot machines, video lottery terminals ("VLTs"), and other gaming machines that print tickets or receipts instead of issuing coins ("ticket-in, ticket-out" or "TITO") at casinos and racetracks ("racinos") and other gaming venues worldwide. Revenue from this market also includes sales of printers used in the international off-premise gaming market in gaming machines such as Amusement with Prizes ("AWP"), Skills with Prizes ("SWP") and Fixed Odds Betting Terminals ("FOBT") at non-casino gaming establishments. Revenue from this market also includes royalties related to our patented casino and gaming technology. In addition, casino and gaming market revenue includes sales of our software solution, the EPICENTRAL™ print system, that enables casino operators to create promotional coupons and marketing messages and to print them real-time at the slot machine. A summary of sales of our worldwide casino and gaming products for the three months ended June 30, 2013 and 2012 is as follows (in thousands, except percentages):

| | Three months ended June 30, 2013 | | Three months ended June 30, 2012 | | Change | |
|----------|-------------------------------------|-------|-------------------------------------|-------|---------|--------|
| | \$ | % | \$ | % | \$ | % |
| Domestic | \$ 3,658 | 50.0% | \$ 3,715 | 52.2% | \$ (57) | (1.5%) |

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| | | | | | | |
|---------------|----------|--------|----------|--------|--------|------|
| International | 3,664 | 50.0% | 3,397 | 47.8% | 267 | 7.9% |
| | \$ 7,322 | 100.0% | \$ 7,112 | 100.0% | \$ 210 | 3.0% |

The decrease in domestic sales of our casino and gaming products is primarily due to a 9% decrease in sales of our thermal casino printers which was almost fully offset by higher EPICENTRAL™ software sales compared to 2012 due to a new installation that occurred in the second quarter of 2013. We believe that our lower casino printer sales during the second quarter of 2013 resulted primarily from fewer new casino openings compared to the second quarter of 2012.

International casino and gaming printer sales increased due primarily to a 34% increase in sales of our off-premise thermal gaming printers mainly from a 77% and 19% increase in sales to customers in Australia and Asia, and our European distributor, respectively. Sales of our off-premise gaming printers are largely project-oriented and we therefore cannot predict the level of future sales. Additionally, sales of our thermal casino printers increased 1% as higher sales to customers in Australia and Asia and our Canadian distributor of 33% and 30%, respectively, were almost fully offset by lower sales to our European distributor.

Lottery:

Revenue from the lottery market includes sales of thermal on-line and other lottery printers to GTECH Corporation (“GTECH”) and its subsidiaries for various lottery applications. A summary of sales of our worldwide lottery printers for the three months ended June 30, 2013 and 2012 is as follows (in thousands, except percentages):

| | Three months ended June 30, 2013 | | Three months ended June 30, 2012 | | Change | |
|---------------|-------------------------------------|--------|-------------------------------------|--------|------------|----------|
| | \$ | % | \$ | % | \$ | % |
| Domestic | \$ 499 | 100.0% | \$ 1,508 | 87.3% | \$ (1,009) | (66.9%) |
| International | - | - % | 220 | 12.7% | (220) | (100.0%) |
| | \$ 499 | 100.0% | \$ 1,728 | 100.0% | \$ (1,229) | (71.1%) |

Our sales to GTECH are directly dependent on the timing and number of new and upgraded lottery terminal installations GTECH performs, and as a result, may fluctuate significantly quarter-to-quarter and year-to-year and are not indicative of GTECH’s overall business or revenue. Based on our backlog of orders and customer’s forecast, we expect total sales to GTECH for 2013 to be approximately \$4 to \$5 million.

Printrex:

Printrex branded printers are sold into markets that include wide format, rack mounted and vehicle mounted black/white and color thermal printers used by customers to log and plot oil field and down hole well drilling data in the oil and gas exploration industry. It also includes high-speed color inkjet desktop printers used to print logs at data centers of the oil and gas field service companies. Revenue in this market also includes sales of wide format printers used to print test results in ophthalmology devices in the medical industry, as well as vehicle mounted printers used to print schematics and certain other critical information in emergency services vehicles. A summary of sales of our worldwide Printrex printers for the three months ended June 30, 2013 and 2012 is as follows (in thousands, except percentages):

| | Three months ended June 30, 2013 | | Three months ended June 30, 2012 | | Change | |
|---------------|-------------------------------------|--------|-------------------------------------|--------|----------|---------|
| | \$ | % | \$ | % | \$ | % |
| Domestic | \$ 971 | 92.5% | \$ 962 | 81.9% | \$ 9 | 0.9% |
| International | 79 | 7.5% | 212 | 18.1% | (133) | (62.7%) |
| | \$ 1,050 | 100.0% | \$ 1,174 | 100.0% | \$ (124) | (10.6%) |

The decrease in Printrex printers is primarily due to lower international sales in both the oil and gas and medical markets, partially offset by higher sales of our new Printrex® 920 color printer in the worldwide oil and gas market.

TSG:

Revenue from TSG includes sales of consumable products (inkjet cartridges, ribbons, receipt paper, color thermal paper and other printing supplies), replacement parts, maintenance and repair services, testing services, refurbished printers, and shipping and handling charges. A summary of sales in our worldwide TSG market for the three months ended June 30, 2013 and 2012 is as follows (in thousands, except percentages):

| | Three months ended June 30, 2013 | | Three months ended June 30, 2012 | | Change | |
|---------------|-------------------------------------|--------|-------------------------------------|--------|--------|---------|
| | \$ | % | \$ | % | \$ | % |
| Domestic | \$ 3,264 | 94.2% | \$ 2,905 | 91.8% | \$ 359 | 12.4% |
| International | 200 | 5.8% | 258 | 8.2% | (58) | (22.5%) |
| | \$ 3,464 | 100.0% | \$ 3,163 | 100.0% | \$ 301 | 9.5% |

The increase in domestic revenue from TSG is primarily due to a 63% increase in sales of replacement parts, higher service sales in addition to revenue contributions from consumables for our new Printrex color printers. These increases were partially offset by lower non-Printrex consumable product sales of 11%. Internationally, TSG revenue decreased due primarily to lower sales of replacement parts and consumable parts as compared to the second quarter of 2012. We expect TSG sales for the full year 2013 to be higher than in 2012 as we expect to benefit from sales of consumables from our newly launched Printrex color oil and gas printers.

12

Gross Profit. Gross profit information is summarized below (in thousands, except percentages):

| Three months ended | | Percent Change | Percent of Total Sales - 2013 | Percent of Total Sales - 2012 |
|--------------------|------------------|-------------------|----------------------------------|----------------------------------|
| 2013 | June 30, 2012 | | | |
| \$ 6,452 | \$ 5,842 | 10.4% | 40.9% | 36.9% |

Gross profit is measured as revenue less cost of sales, which includes primarily the cost of all raw materials and component parts, direct labor, manufacturing overhead expenses, cost of finished products purchased directly from our contract manufacturers and expenses associated with installations of our EPICENTRAL® print system. Gross profit increased \$610,000, or 10%, and our gross margin significantly improved by 400 basis points as we continued to transition our business towards a more favorable sales mix of value-added products. During the second quarter of 2013, our gross margin primarily benefited from sales contributions of our new Ithaca® 9700 food safety terminal in addition to EPICENTRAL™ software sales. We expect our gross margin for the remainder of 2013 to be higher than in 2012 as we expect to continue to benefit from increased sales of our new value-added products.

Engineering, Design and Product Development. Engineering, design and product development information is summarized below (in thousands, except percentages):

| Three months ended | | Percent Change | Percent of Total Sales - 2013 | Percent of Total Sales - 2012 |
|--------------------|------------------|-------------------|----------------------------------|----------------------------------|
| 2013 | June 30, 2012 | | | |
| \$ 995 | \$ 952 | 4.5% | 6.3% | 6.0% |

Engineering, design and product development expenses primarily include salary and payroll related expenses for our engineering staff, depreciation and design expenses (including prototype printer expenses, outside design and testing services, and supplies). Such expenses increased \$43,000, or 5%, due primarily to higher compensation-related expenses for existing engineering staff from annual salary increases.

Selling and Marketing. Selling and marketing information is summarized below (in thousands, except percentages):

| Three months ended | | Percent Change | Percent of Total Sales - 2013 | Percent of Total Sales - 2012 |
|--------------------|------------------|-------------------|----------------------------------|----------------------------------|
| 2013 | June 30, 2012 | | | |
| \$ 1,857 | \$ 1,674 | 10.9% | 11.8% | 10.6% |

Selling and marketing expenses primarily include salaries and payroll related expenses for our sales and marketing staff, sales commissions, travel expenses, expenses associated with the lease of sales offices, advertising, trade show expenses, e-commerce and other promotional marketing expenses. Such expenses increased by \$183,000, or 11%, in the second quarter of 2013 compared to the second quarter of 2012 primarily due to the addition of new sales staff and increased marketing spend to support our newly launched products. We expect selling and marketing expenses to be higher in 2013 than in 2012 due to expansion of our sales staff and higher trade show and promotional marketing expenses as we continue to focus our selling and marketing efforts on our new, value-added products.

General and Administrative. General and administrative information is summarized below (in thousands, except percentages):

| Three months ended | | Percent Change | Percent of Total Sales - 2013 | Percent of Total Sales - 2012 |
|--------------------|------------------|-------------------|----------------------------------|----------------------------------|
| 2013 | June 30, 2012 | | | |
| \$ 1,736 | \$ 1,903 | (8.8%) | 11.0% | 12.0% |

General and administrative expenses primarily include salaries and payroll related expenses for our executive, accounting, human resource, business development and information technology staff, expenses for our corporate headquarters, professional and legal expenses, telecommunication expenses, and other expenses related to being a publicly-traded company. General and administrative expenses decreased \$167,000, or 9%, due primarily to a reduction in the accrued contingent consideration liability to be paid in connection with the acquisition of Printrex as discussed in Note 4 to the Condensed Consolidated Financial Statements. We expect general and administrative expenses in 2013 to be relatively consistent with 2012.

Legal Fees Associated with Lawsuit. Legal fee information is summarized below (in thousands, except percentages):

| Three months ended | | Percent Change | Percent of Total Sales - 2013 | Percent of Total Sales - 2012 |
|--------------------|------------------|-------------------|----------------------------------|----------------------------------|
| 2013 | June 30, 2012 | | | |
| \$ 57 | \$ 471 | (87.9%) | 0.4% | 3.0% |

As disclosed in Note 9 to the Condensed Consolidated Financial Statements, in June 2012, Avery Dennison Corporation filed a civil complaint against the Company. In connection with this lawsuit, we incurred legal fees and other related expenses of \$57,000 and \$471,000, respectively, in the second quarter of 2013 and 2012. We may incur additional legal fees related to this lawsuit for the remainder of 2013 and beyond, although we cannot predict the timing and extent of such legal fees.

Business Consolidation and Restructuring. Business consolidation and restructuring information is summarized below (in thousands, except percentages):

| Three months ended | | Percent Change | Percent of Total Sales - 2013 | Percent of Total Sales - 2012 |
|--------------------|------------------|-------------------|----------------------------------|----------------------------------|
| 2013 | June 30, 2012 | | | |
| \$ - | \$ 63 | (100.0%) | - % | 0.4% |

As disclosed in Note 8 to the Condensed Consolidated Financial Statements, in January 2012, we determined that we no longer needed to maintain the existing Printrex manufacturing facility in San Jose, California, along with certain redundant headcount. During the three months ended June 30, 2012, we recorded a restructuring charge of \$63,000 for employee termination benefits related to these employee reductions as well as moving costs. We did not incur any restructuring charges in the second quarter of 2013.

Operating Income. Operating income information is summarized below (in thousands, except percentages):

| Three months ended | | Percent Change | Percent of Total Sales - 2013 | Percent of Total Sales - 2012 |
|--------------------|------------------|-------------------|----------------------------------|----------------------------------|
| 2013 | June 30, 2012 | | | |
| \$ 1,807 | \$ 779 | 132.0% | 11.4% | 4.9% |

Our operating income increased primarily due to a 400 basis point improvement in gross margin in the second quarter of 2013 as compared to the second quarter of 2012. In addition, both our operating profit and operating margin for the second quarter of 2013 were favorably impacted by lower legal fees incurred in connection with the AD lawsuit as compared to the second quarter of 2012 by \$414,000 or approximately 260 basis points.

Interest. Interest expense and interest income fully offset in the second quarter of 2013 compared to net interest income of \$2,000 recorded in the second quarter of 2012. Interest expense related to the unused revolving credit line fee and amortization of deferred financing costs on our revolving credit facility with TD Bank N.A. ("TD Bank") remained consistent in the second quarter of 2013 compared to the second quarter of 2012. See "Liquidity and Capital Resources" below for more information.

Other, net. We recorded other expenses of \$4,000 in the second quarter of 2013 compared to other income of \$13,000 in the second quarter of 2012. The change was due to foreign currency transaction exchange losses recorded by our U.K. subsidiary in the second quarter of 2013 compared to gains recorded in the second quarter of 2012.

Income Taxes. We recorded an income tax provision for the second quarter of 2013 of \$588,000 at an effective tax rate of 32.6%, compared to an income tax provision during the second quarter of 2012 of \$286,000 at an effective tax rate of 36.0%. Our effective tax rate for the second quarter of 2013 is lower than the second quarter of 2012 primarily because it includes the benefit from the federal research and development (“R&D”) credit which was not included in the 2012 income tax provision since it expired at the end of 2011. For the remainder of 2013, we expect our annual effective tax rate to be between 33% and 34%.

Net Income. We reported net income during the second quarter of 2013 of \$1,215,000, or \$0.14 per diluted share, compared to \$508,000, or \$0.06 per diluted share, for the second quarter of 2012.

Results of Operations: Six months ended June 30, 2013 compared to six months ended June 30, 2012

Net Sales. Net sales, which include printer, terminal and software sales as well as sales of replacement parts, consumables and maintenance and repair services, by market for the six months ended June 30, 2013 and 2012 were as follows (in thousands, except percentages):

| | Six months ended June 30, 2013 | | Six months ended June 30, 2012 | | Change | |
|---------------------------------|-----------------------------------|--------|-----------------------------------|--------|------------|---------|
| | \$ | % | \$ | % | \$ | % |
| Food safety, banking and POS | \$ 5,437 | 17.6% | \$ 5,012 | 15.0% | \$ 425 | 8.5% |
| Casino and gaming | 14,062 | 45.6% | 16,523 | 49.5% | (2,461) | (14.9%) |
| Lottery | 1,864 | 6.0% | 2,758 | 8.2% | (894) | (32.4%) |
| Printrex | 2,375 | 7.7% | 2,413 | 7.2% | (38) | (1.6%) |
| TSG | 7,107 | 23.1% | 6,706 | 20.1% | 401 | 6.0% |
| | \$ 30,845 | 100.0% | \$ 33,412 | 100.0% | \$ (2,567) | (7.7%) |
| International * | \$ 7,328 | 23.8% | \$ 10,480 | 31.4% | \$ (3,152) | (30.1%) |

* International sales do not include sales of printers made to domestic distributors or other domestic customers who may in turn ship those printers to international destinations.

Net sales for the first half of 2013 decreased \$2,567,000, or 8%, from the same period in 2012. Printer sales volume decreased 21% to approximately 75,000 units driven primarily by unit volume decreases of 20%, 35% and 17% from the casino and gaming, lottery and food safety, banking and POS markets, respectively. Despite lower sales volume in the first half of 2013, the average selling price of our printers increased approximately 9% compared to the first half of 2012 primarily due to 1) significant sales contributions of our new Ithaca ® 9700 food safety terminal and 2) lower sales of lottery and POS printers which have lower average selling prices than other printers. Overall, international sales decreased \$3,152,000, or 30%, primarily driven by lower sales to the casino and gaming market.

Food safety, banking and POS:

A summary of sales of our worldwide food safety, banking and POS products for the six months ended June 30, 2013 and 2012 is as follows (in thousands, except percentages):

| | Six months ended June 30, 2013 | | Six months ended June 30, 2012 | | Change | |
|---------------|-----------------------------------|--------|-----------------------------------|--------|--------|---------|
| | \$ | % | \$ | % | \$ | % |
| Domestic | \$ 5,302 | 97.5% | \$ 4,776 | 95.3% | \$ 526 | 11.0% |
| International | 135 | 2.5% | 236 | 4.7% | (101) | (42.8%) |
| | \$ 5,437 | 100.0% | \$ 5,012 | 100.0% | \$ 425 | 8.5% |

The increase in domestic food safety, banking and POS printer revenue as compared to the first half of 2012 was primarily driven by significant sales from our new Ithaca ® 9700 food safety terminal during the first half of 2013. This was partially offset by lower sales of our banking printers mainly due to the shipment of a large order for our Ithaca® 280 thermal receipt printer to a banking customer in the first half of 2012 that did not repeat in the same period in 2013.

Casino and gaming:

A summary of sales of our worldwide casino and gaming products for the six months ended June 30, 2013 and 2012 is as follows (in thousands, except percentages):

| | Six months ended | | Six months ended | | Change | |
|---------------|------------------|--------|------------------|--------|------------|---------|
| | June 30, 2013 | | June 30, 2012 | | \$ | % |
| Domestic | \$ 7,560 | 53.8% | \$ 7,542 | 45.6% | \$ 18 | 0.2% |
| International | 6,502 | 46.2% | 8,981 | 54.4% | (2,479) | (27.6%) |
| | \$ 14,062 | 100.0% | \$ 16,523 | 100.0% | \$ (2,461) | (14.9%) |

The slight increase in domestic sales of our casino and gaming products is primarily due to higher EPICENTRAL™ software sales due to three new installations that occurred in the first half of 2013 which was almost fully offset by a 13% decrease in sales of our thermal casino printers. We believe that our lower casino printer sales during the first half of 2013 resulted primarily from fewer new casino openings compared to the first half of 2012.

International casino and gaming printer sales decreased in the first half of 2013 due primarily to a 52% decrease in sales of our off-premise thermal gaming printers mainly from a 55% decrease in sales to our European distributor. Sales of our off-premise gaming printers are largely project-oriented and we therefore cannot predict the level of future sales. Additionally, sales of our thermal casino printers decreased by 17% primarily from lower sales to our European and Canadian distributors of 27% and 28%, respectively. This decline in sales of our thermal casino printers resulted primarily from fewer installations of VLT gaming machines in Italy as the government approved rollout of these games was substantially completed during 2012, and we therefore expect to ship fewer printers in 2013.

Lottery:

A summary of sales of our worldwide lottery printers for the six months ended June 30, 2013 and 2012 is as follows (in thousands, except percentages):

| | Six months ended June 30, 2013 | | Six months ended June 30, 2012 | | Change | |
|---------------|-----------------------------------|--------|-----------------------------------|--------|----------|---------|
| | \$ | % | \$ | % | \$ | % |
| Domestic | \$ 1,833 | 98.3% | \$ 2,523 | 91.5% | \$ (690) | (27.3%) |
| International | 31 | 1.7% | 235 | 8.5% | (204) | (86.8%) |
| | \$ 1,864 | 100.0% | \$ 2,758 | 100.0% | \$ (894) | (32.4%) |

Our sales to GTECH are directly dependent on the timing and number of new and upgraded lottery terminal installations GTECH performs, and as a result, may fluctuate significantly quarter-to-quarter and year-to-year and are not indicative of GTECH's overall business or revenue. Based on our backlog of orders and customer's forecast, we expect total sales to GTECH for 2013 to be approximately \$4 to \$5 million.

Printrex:

A summary of sales of our worldwide Printrex printers for the six months ended June 30, 2013 and 2012 is as follows (in thousands, except percentages):

| | Six months ended June 30, 2013 | | Six months ended June 30, 2012 | | Change | |
|---------------|-----------------------------------|--------|-----------------------------------|--------|---------|---------|
| | \$ | % | \$ | % | \$ | % |
| Domestic | \$ 2,126 | 89.5% | \$ 2,037 | 84.4% | \$ 89 | 4.4% |
| International | 249 | 10.5% | 376 | 15.6% | (127) | (33.8%) |
| | \$ 2,375 | 100.0% | \$ 2,413 | 100.0% | \$ (38) | (1.6%) |

The decrease in Printrex printers is primarily due to lower international sales in both the oil and gas and medical and mobile markets, partially offset by higher sales of our two new color printers in the worldwide oil and gas market, the Printrex® 920 and Printrex® 980.

TSG:

A summary of sales in our worldwide TSG market for the six months ended June 30, 2013 and 2012 is as follows (in thousands, except percentages):

| | Six months ended June 30, 2013 | | Six months ended June 30, 2012 | | Change | |
|---------------|-----------------------------------|--------|-----------------------------------|--------|--------|---------|
| | \$ | % | \$ | % | \$ | % |
| Domestic | \$ 6,696 | 94.2% | \$ 6,054 | 90.3% | \$ 642 | 10.6% |
| International | 411 | 5.8% | 652 | 9.7% | (241) | (37.0%) |
| | \$ 7,107 | 100.0% | \$ 6,706 | 100.0% | \$ 401 | 6.0% |

The increase in domestic revenue from TSG is primarily due to a 70% increase in sales of replacement parts in addition to higher service sales and sales of consumables for our new Printrex color printers. These increases were largely offset by lower non-Printrex consumable product sales of 16%. Internationally, TSG revenue decreased due primarily to lower sales of replacement parts and accessories as compared to the first half of 2012. We expect TSG sales for the full year 2013 to be higher than in 2012 as we expect to benefit from sales of consumables from our newly launched Printrex color oil and gas printers.

Gross Profit. Gross profit information is summarized below (in thousands, except percentages):

| Six months ended | | Percent Change | Percent of Total Sales - 2013 | Percent of Total Sales - 2012 |
|------------------|------------------|-------------------|----------------------------------|----------------------------------|
| 2013 | June 30, 2012 | | | |
| \$ 12,885 | \$ 12,620 | 2.1% | 41.8% | 37.8% |

While gross profit modestly increased, our gross margin significantly improved by 400 basis points as we continued to transition our business towards a more favorable sales mix of value-added products. During the first half of 2013, our gross margin primarily benefited from sales contributions of our new Ithaca® 9700 food safety terminal in addition to three EPICENTRAL™ software installations. We expect our gross margin for the remainder of 2013 to be higher than in 2012 as we expect to continue to benefit from increased sales of our new value-added products.

Engineering, Design and Product Development. Engineering, design and product development information is summarized below (in thousands, except percentages):

| Six months ended | | Percent Change | Percent of Total Sales - 2013 | Percent of Total Sales - 2012 |
|------------------|------------------|-------------------|----------------------------------|----------------------------------|
| 2013 | June 30, 2012 | | | |
| \$ 2,007 | \$ 2,165 | (7.3%) | 6.5% | 6.5% |

Such expenses decreased \$158,000, or 7%, which was due primarily to lower outside testing and pre-production expenses related to the four new products that were launched in 2012.

Selling and Marketing. Selling and marketing information is summarized below (in thousands, except percentages):

| Six months ended | | Percent Change | Percent of Total Sales - 2013 | Percent of Total Sales - 2012 |
|------------------|------------------|-------------------|----------------------------------|----------------------------------|
| 2013 | June 30, 2012 | | | |
| \$ 3,643 | \$ 3,275 | 11.2% | 11.8% | 9.8% |

Such expenses increased by \$368,000, or 11%, in the first half of 2013 compared to the first half of 2012 primarily due to the addition of new sales staff and increased marketing spend to support our newly launched products. We expect selling and marketing expenses to be higher in 2013 than in 2012 due to expansion of our sales staff and higher trade show and promotional marketing expenses as we continue to focus our selling and marketing efforts on our new, value-added products.

General and Administrative. General and administrative information is summarized below (in thousands, except percentages):

| Six months ended | | Percent Change | Percent of Total Sales - 2013 | Percent of Total Sales - 2012 |
|------------------|------------------|-------------------|----------------------------------|----------------------------------|
| 2013 | June 30, 2012 | | | |
| \$ 3,770 | \$ 3,903 | (3.4%) | 12.2% | 11.7% |

General and administrative expenses decreased \$133,000, or 3%, due primarily to a reduction in the accrued contingent consideration liability to be paid in connection with the acquisition of Printrex as discussed in Note 4 to the

Condensed Consolidated Financial Statements. We expect general and administrative expenses in 2013 to be relatively consistent with 2012.

Legal Fees Associated with Lawsuit. Legal fee information is summarized below (in thousands, except percentages):

| Six months ended | | Percent Change | Percent of Total Sales - 2013 | Percent of Total Sales - 2012 |
|------------------|------------------|-------------------|----------------------------------|----------------------------------|
| 2013 | June 30, 2012 | | | |
| \$ 256 | \$ 471 | (45.7%) | 0.8% | 1.4% |

As disclosed in Note 9 to the Condensed Consolidated Financial Statements, in June 2012, Avery Dennison Corporation filed a civil complaint against the Company. In connection with this lawsuit, we incurred legal fees and other related expenses of \$256,000 and \$471,000, respectively, in the first six months of 2013 and 2012. We may incur additional legal fees related to this lawsuit for the remainder of 2013 and beyond, although we cannot predict the timing and extent of such legal fees.

Business Consolidation and Restructuring. Business consolidation and restructuring information is summarized below (in thousands, except percentages):

| Six months ended | | Percent Change | Percent of Total Sales - 2013 | Percent of Total Sales - 2012 |
|------------------|---------------|----------------|-------------------------------|-------------------------------|
| 2013 | June 30, 2012 | | | |
| \$ - | \$ 117 | (100.0%) | - % | 0.4% |

As disclosed in Note 8 to the Condensed Consolidated Financial Statements, in January 2012, we determined that we no longer needed to maintain the existing Printrex manufacturing facility in San Jose, California, along with certain redundant headcount. During the six months ended June 30, 2012, we recorded a restructuring charge of \$117,000 for employee termination benefits related to these employee reductions as well as moving costs. We did not incur any restructuring charges in the first six months of 2013.

Operating Income. Operating income information is summarized below (in thousands, except percentages):

| Six months ended | | Percent Change | Percent of Total Sales - 2013 | Percent of Total Sales - 2012 |
|------------------|---------------|----------------|-------------------------------|-------------------------------|
| 2013 | June 30, 2012 | | | |
| \$ 3,209 | \$ 2,689 | 19.3% | 10.4% | 8.0% |

Our operating income increased primarily from the 400 basis point improvement in gross margin in the first half of 2013 as compared to the first half of 2012. Additionally, lower legal fees in connection with the AD lawsuit and no restructuring charges in the first half of also improved both operating income and operating margin by \$332,000 and approximately 110 basis points, respectively. These increases were partially offset by an 8% lower sales volume as well as higher selling and marketing expenses in the first half of 2013.

Interest. We recorded net interest expense of \$1,000 in the first half of 2013 compared to net interest income of \$4,000 in the first half of 2012. Interest expense related to the unused revolving credit line fee and amortization of deferred financing costs on our revolving credit facility with TD Bank remained consistent in the first half of 2013 compared to the first half of 2012. See "Liquidity and Capital Resources" below for more information.

Other, net. We recorded other income of \$33,000 in the first half of 2013 compared to other expenses of \$11,000 in the first half of 2012. The change was due to foreign currency transaction exchange gains recorded by our U.K. subsidiary in the first half of 2013 compared to losses recorded in the first half of 2012.

Income Taxes. We recorded an income tax provision for the first six months of 2013 of \$866,000 at an effective tax rate of 26.7%, compared to an income tax provision during the first six months of 2012 of \$966,000 at an effective tax rate of 36.0%. Our effective tax rate for the first six months of 2013 is unusually low because it includes the full-year benefit from the 2012 federal research and development ("R&D") credit of approximately \$220,000 as this credit was not renewed until January 2, 2013 as a component of the American Taxpayer Relief Act of 2012 (the "Act"). For the remainder of 2013, we expect our annual effective tax rate to be between 33% and 34%.

Net Income. We reported net income during the first six months of 2013 of \$2,375,000, or \$0.27 per diluted share, compared to \$1,716,000, or \$0.18 per diluted share, for the first six months of 2012.

18

Liquidity and Capital Resources

Cash Flow

In the first six months of 2013, our cash and cash equivalents balance increased \$1,291,000, or 17%, from December 31, 2012 and we ended the second quarter of 2013 with \$8,828,000 in cash and cash equivalents and no debt outstanding even after returning \$2,014,000 to shareholders in the form of cash dividends paid on common stock and treasury share repurchases during the first six months of 2013.

Operating activities: The following significant factors affected our cash provided by operating activities of \$3,307,000 in the first six months of 2013 as compared to our cash provided by operating activities of \$5,671,000 in the first six months of 2012:

During the first six months of 2013:

- We reported net income of \$2,375,000.
- We recorded depreciation, amortization, and non-cash compensation expense of \$1,162,000, including \$156,000 of amortization related to intangible assets acquired from Printrex.
- Accounts receivable decreased \$4,277,000 due primarily to collections made from the high concentration of sales made during the latter portion of the fourth quarter of 2012.
- Inventories increased \$2,467,000 as we continue to increase stocking levels of our new food safety and Printrex products in anticipation of higher expected sales volume.
- Accounts payable decreased \$818,000 due primarily to higher payments during the period from inventory purchased in the first six months of 2013 to support the higher expected sales volume of our new products for the remainder of the year.
- Accrued liabilities and other liabilities decreased \$990,000 due primarily to the payment of 2012 annual bonuses in March 2013.

During the first six months of 2012:

- We reported net income of \$1,716,000.
- We recorded depreciation, amortization, and non-cash compensation expense of \$1,169,000, including \$190,000 of amortization related to intangible assets acquired from Printrex.
- Accounts receivable increased \$2,072,000 due to a higher concentration of sales made during the latter portion of the second quarter.
- Inventories decreased \$2,500,000 due to our continued effort to reduce inventory purchases and to fulfill sales with existing inventory stock.
- Accounts payable increased \$1,853,000 due primarily to the timing of payments during the latter portion of the second quarter.
- Accrued liabilities and other liabilities increased \$580,000 due primarily to higher accrued legal fees primarily in connection with the Avery Dennison lawsuit as disclosed in Note 9 to the Condensed Consolidated Financial Statements in addition to deferred revenue associated with new contracts for paper qualification testing entered into during the first half of the year.

Investing activities: Our capital expenditures were \$426,000 and \$339,000 in the first six months of 2013 and 2012, respectively. Expenditures in 2013 included approximately \$89,000 for costs incurred in connection with an upgrade to the Company's ERP software and the remaining amount primarily for the purchase of new product tooling and computer equipment. Expenditures in 2012 included \$79,000 for the purchase of computer equipment and the remaining amount primarily for the purchase of new product tooling. Additionally, our capitalized software development costs were \$42,000 and \$10,000 in the first six months of 2013 and 2012, respectively, all of which was related to our EPICENTRAL™ print system.

Capital expenditures, including capitalized software development costs, for 2013 are expected to be approximately \$1,000,000 primarily for new product tooling and tooling enhancements for our existing products.

Financing activities: We used \$1,535,000 of cash from financing activities during the first six months of 2013 to pay cash dividends of \$1,127,000 to common shareholders and to purchase \$887,000 of common stock for treasury, partially offset by proceeds and tax benefits from stock option exercises of \$479,000. During the first six months of 2012, we used \$4,964,000 of cash from financing activities to repurchase \$5,151,000 of Company stock partially offset by proceeds and tax benefits from stock option exercises of \$187,000.

Working Capital

Our working capital increased 5% to \$26,822,000 at June 30, 2013 from \$25,492,000 at December 31, 2012. Our current ratio of current assets to current liabilities also increased to 4.1 as of June 30, 2013 compared to 3.5 at December 31, 2012. The increase in our working capital and current ratio was largely due to higher cash and cash equivalent and inventory balances and lower accounts payable and accrued expenses partially offset by lower accounts receivable balances.

Credit Facility and Borrowings

We maintain a credit facility (the “TD Bank Credit Facility”) with TD Bank which provides for a \$20,000,000 revolving credit line that expires on November 28, 2014. Borrowings under the TD Bank Credit Facility bear a floating rate of interest at the prime rate minus one percent and are secured by a lien on all of our assets. We also pay a fee of 0.25% on unused borrowings under the TD Bank Credit Facility.

On September 7, 2012, we signed an amendment to the TD Bank Credit Facility that allows us to declare and pay cash dividends to holders of our outstanding common shares subject to approval by our Board of Directors and provided that no default or event of default has occurred and is continuing under the credit facility on the date of the dividend payment. The amendment also allows us to use up to \$5,000,000 in revolving credit loans to fund future cash dividend payments or treasury share buybacks as well as requires cash dividend payments to be treated as distributions for purposes of quarterly debt covenant calculations.

The TD Bank Credit Facility imposes certain quarterly financial covenants on us and restricts, among other things, our ability to incur additional indebtedness and the creation of other liens. We were in compliance with all financial covenants of the TD Bank Credit Facility at June 30, 2013. The following table lists the financial covenants and the performance measurements at June 30, 2013:

| Financial Covenant | Requirement/Restriction | Calculation at June 30, 2013 |
|--|-------------------------|------------------------------|
| Operating cash flow / Total debt service | Minimum of 1.25 times | 101.7 times |
| Funded Debt / EBITDA | Maximum of 3.0 times | 0 times |

As of June 30, 2013, undrawn commitments under the TD Bank Credit facility were \$20,000,000.

Shareholder Dividend Payments

On September 10, 2012, we announced that our Board of Directors approved the initiation of a quarterly cash dividend program which is subject to the Board’s approval each quarter. On May 2, 2013, our Board of Directors declared an increase to the quarterly cash dividend from \$0.06 per share to \$0.07 per share. For the three months ended June 30, 2013, our Board of Directors declared a quarterly cash dividend of \$0.07 per share, totaling approximately \$608,000, which was paid in June 2013 to common shareholders of record at the close of business on May 20, 2013. For the six months ended June 30, 2013, dividends declared and paid totaled \$1,127,000, or \$0.13 per share. We expect to pay approximately \$2,400,000 in cash dividends to our common shareholders during 2013.

Stock Repurchase Program

Prior to its expiration on May 27, 2013, we maintained a stock repurchase program (the “Stock Repurchase Program”) whereby we were authorized to repurchase up to \$15,000,000, as increased from \$10,000,000 in March 2012, of our outstanding shares of common stock from time to time in the open market, depending on market conditions, share price and other factors. The Stock Repurchase Program expired on May 27, 2013 and was not renewed. During the six months ended June 30, 2013, we repurchased 114,161 shares of our common stock for approximately \$887,000 at an average price per share of \$7.77. As of June 30, 2013, no additional shares are authorized for future repurchases due to the expiration of the Stock Repurchase Program.

Resource Sufficiency

We believe that our cash and cash equivalents on hand and cash flows generated from operating activities will provide sufficient resources to meet our working capital needs, finance our capital expenditures and dividend payments and meet our liquidity requirements through at least the next twelve months.

Contractual Obligations / Off-Balance Sheet Arrangements

The disclosure of payments we have committed to make under our contractual obligations is set forth under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations—Contractual Obligations" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2012. There have been no material changes in our contractual obligations outside the ordinary course of business since December 31, 2012. We have no material off-balance sheet arrangements as defined in Regulation S-K 303(a)(4)(ii).

Item 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The disclosure of our exposure to market risk is set forth under the heading "Quantitative and Qualitative Disclosures about Market Risk" in our Annual Report on Form 10-K for the fiscal year ended December 31, 2012. There has been no material change in our exposure to market risk during the six months ended June 30, 2013.

20

Item 4. CONTROLS AND PROCEDURES

The Company, under the supervision and with the participation of its management, including the Chief Executive Officer and the Chief Financial Officer, evaluated the effectiveness of the design and operation of the Company's "disclosure controls and procedures" (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the "Exchange Act")) as of the end of the period covered by this report. Based on that evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of June 30, 2013. There has been no change in the Company's internal control over financial reporting during the quarter ended June 30, 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 1. LEGAL PROCEEDINGS

On June 8, 2012, Avery Dennison Corporation ("AD") filed a civil complaint against the Company and a former employee of the Company and of AD, in the Court of Common Pleas (the "Court") in Lake County, Ohio. The complaint alleges that this former employee and the Company misappropriated unspecified trade secrets and confidential information related to the design of our food safety terminals from AD. The complaint requests a preliminary and permanent injunction against the Company from manufacturing and selling our Ithaca® 9700 and 9800 food safety terminals. On July 16, 2012, the Company filed its answer, affirmative defenses and counterclaims, seeking all available damages including legal fees. A hearing on the plaintiff's motion for preliminary injunction took place in August 2012, and in November 2012, the Court denied this request. AD filed an appeal of the Court's ruling to the Eleventh Appellate District, which heard oral arguments on the appeal on July 16, 2013. On July 23, 2013, AD requested that the Eleventh Appellate District enjoin the Company's further sale and marketing of the food safety terminals, pending the appeals court's decision. On July 29, 2013, TransAct opposed this request. The rulings by the Eleventh District of Appeals on both the appeal and request are pending.

Item 1A. RISK FACTORS

Information regarding risk factors appears in Item 1A of our Annual Report on Form 10-K for the year ended December 31, 2012. There have been no material changes from the risk factors previously disclosed in that Annual Report on Form 10-K. The risks described in our Annual Report on Form 10-K are not the only risks facing our Company. Additional risks and uncertainties not currently known to us or that we currently deem to be immaterial also may materially adversely affect our business, financial condition or future results.

Item 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

ISSUER PURCHASES OF EQUITY SECURITIES

On May 27, 2013, the Stock Repurchase Program expired and was not renewed. During the six months ended June 30, 2013, we repurchased 114,161 shares of our common stock for approximately \$887,000 at an average price per share of \$7.77. As of June 30, 2013, no additional shares are authorized for future repurchases due to the expiration of the Stock Repurchase Program. For additional information, see the discussion under "Management's Discussion and Analysis of Financial Condition and Results of Operations — Liquidity and Capital Resources — Stock Repurchase Program," above. The following table summarizes the repurchase of our common stock in the six months ended June 30, 2013:

| Period | Total Number of Shares Purchased | Average Price Paid per Share | Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | Approximate Dollar Value of Shares that May Yet Be Purchased under the May 2010 Program |
|--------------------------------------|---|------------------------------------|--|--|
| January 1, 2013 – January 31, 2013 | 45,177 | \$ 7.59 | 45,177 | \$ 5,863,000 |
| February 1, 2013 – February 28, 2013 | 23,339 | 8.06 | 23,339 | \$ 5,675,000 |
| March 1, 2013 – March 31, 2013 | 20,384 | 7.89 | 20,384 | \$ 5,514,000 |
| April 1, 2013 – April 30, 2013 | 22,494 | 7.75 | 22,494 | \$ 5,340,000 |
| May 1, 2013 – May 31, 2013 | 2,767 | 7.48 | 2,767 | \$ - * |
| June 1, 2013 – June 30, 2013 | - | - | - | \$ - * |
| Total | 114,161 | \$ 7.77 | 114,161 | |

* - Stock Repurchase Program expired on May 27, 2013

Item 3. DEFAULTS UPON SENIOR SECURITIES

None.

Item 4. MINE SAFETY DISCLOSURES

Not applicable.

Item 5. OTHER INFORMATION

None.

21

Item 6. EXHIBITS

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

TRANSACT TECHNOLOGIES
INCORPORATED
(Registrant)

August 7, 2013

/s/ Steven A. DeMartino
Steven A. DeMartino
President, Chief Financial Officer,
Treasurer and Secretary
(Principal Financial Officer)

/s/ Chad R. Albano
Chad R. Albano
Chief Accounting Officer and
Corporate Controller
(Principal Accounting Officer)

EXHIBIT LIST

The following exhibits are filed herewith.

Exhibit

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