

NATIONAL PRESTO INDUSTRIES INC
Form 10-Q
August 11, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF
1934 FOR THE QUARTERLY PERIOD ENDED July 2, 2017

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 1-2451

NATIONAL PRESTO INDUSTRIES, INC.

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(Exact name of registrant as specified in its charter)

WISCONSIN 39-0494170
(State or other jurisdiction of incorporation (I.R.S. Employer Identification No.)

or organization)

3925 NORTH HASTINGS WAY
EAU CLAIRE, WISCONSIN 54703-3703
(Address of principal executive offices) (Zip Code)

(Registrant's telephone number, including area code) 715-839-2121

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 Website, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company
Emerging growth
company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

There were 6,965,043 shares of the Issuer's Common Stock outstanding as of August 1, 2017.

PART I – FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

NATIONAL PRESTO INDUSTRIES, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

July 2, 2017 and December 31, 2016

(Dollars in thousands)

	July 2, 2017 (Unaudited)	December 31, 2016	
ASSETS			
CURRENT ASSETS:			
Cash and cash equivalents	\$ 10,026	\$ 27,034	
Marketable securities	128,706	84,457	
Accounts receivable, net	38,056	67,285	
Inventories:			
Finished goods	\$ 29,211	\$ 25,200	
Work in process	83,178	66,528	
Raw materials	4,511	116,900	3,675
Assets held for sale		5,335	58,893
Other current assets		7,028	7,423
Total current assets		306,051	340,495
PROPERTY, PLANT AND EQUIPMENT	\$ 103,552	\$ 101,163	
Less allowance for depreciation	55,428	48,124	51,688
GOODWILL		11,485	11,485
INTANGIBLE ASSETS, net		4,589	4,961
NOTES RECEIVABLE		6,642	6,534
DEFERRED INCOME TAXES		4,910	-
OTHER ASSETS		8,138	4,644
	\$ 389,939	\$ 417,594	

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

NATIONAL PRESTO INDUSTRIES, INC. AND SUBSIDIARIES
 CONDENSED CONSOLIDATED BALANCE SHEETS
 July 2, 2017 and December 31, 2016
 (Dollars in thousands)

	July 2, 2017 (Unaudited)	December 31, 2016
LIABILITIES AND STOCKHOLDERS' EQUITY		
LIABILITIES		
CURRENT LIABILITIES:		
Accounts payable	\$ 31,175	\$ 39,584
Federal and state income taxes	5,579	6,273
Accrued liabilities	12,342	12,244
Liabilities held for sale	17	6,253
Total current liabilities	49,113	64,354
DEFERRED INCOME TAXES	-	3,004
COMMITMENTS AND CONTINGENCIES		
STOCKHOLDERS' EQUITY		
Common stock, \$1 par value:		
Authorized: 12,000,000 shares		
Issued: 7,440,518 shares	\$ 7,441	\$ 7,441
Paid-in capital	8,650	7,913
Retained earnings	339,666	350,203
Accumulated other comprehensive (loss)	(24)	(47)
	355,733	365,510
Treasury stock, at cost	14,907	15,274
Total stockholders' equity	340,826	350,236
	\$ 389,939	\$ 417,594

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

NATIONAL PRESTO INDUSTRIES, INC. AND SUBSIDIARIES
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

Three and Six Months Ended July 2, 2017 and July 3, 2016

(Unaudited)

(In thousands except per share data)

	Three Months Ended		Six Months Ended	
	2017	2016	2017	2016
Net sales	\$ 74,561	\$ 69,516	\$ 147,415	\$ 135,458
Cost of sales	57,001	52,349	109,729	102,243
Gross profit	17,560	17,167	37,686	33,215
Selling and general expenses	5,418	5,614	11,178	11,441
Intangibles amortization	5	-	372	568
Operating profit	12,137	11,553	26,136	21,206
Other income	980	188	1,930	371
Earnings from continuing operations before provision for income taxes	13,117	11,741	28,066	21,577
Provision for income taxes from continuing operations	4,176	3,805	9,152	7,131
Earnings from continuing operations	\$ 8,941	\$ 7,936	\$ 18,914	\$ 14,446
Earnings from discontinued operations, net of tax	771	338	8,953	1,039
Net earnings	\$ 9,712	\$ 8,274	\$ 27,867	\$ 15,485
Weighted average shares outstanding:				
Basic and diluted	6,990	6,970	6,985	6,967
Earnings per share, basic and diluted:				
From continuing operations	\$ 1.28	\$ 1.14	\$ 2.71	2.07
From discontinued operations	0.11	0.05	1.28	0.15
Net earnings per share	\$ 1.39	\$ 1.19	\$ 3.99	\$ 2.22
Comprehensive income:				
Net earnings	\$ 9,712	\$ 8,274	\$ 27,867	\$ 15,485
Other comprehensive income, net of tax:				
Unrealized gain (loss) on available-for-sale securities	(5)	13	23	18
Comprehensive income	\$ 9,707	\$ 8,287	\$ 27,890	\$ 15,503
Cash dividends declared and paid per common share	\$ 0.00	\$ 0.00	\$ 5.50	\$ 5.05

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

NATIONAL PRESTO INDUSTRIES, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

Six Months Ended July 2, 2017 and July 3, 2016

(Unaudited)

(Dollars in thousands)

	2017	2016
Cash flows from operating activities:		
Net earnings	\$ 27,867	\$ 15,485
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Provision for depreciation	3,912	5,897
Intangibles amortization	372	568
Provision for doubtful accounts	14	8
Non-cash retirement plan expense	357	374
Gain on involuntary conversion of machinery and equipment	(1,997)	-
Gain on disposal of property, plant and equipment	(2)	-
Gain on divestiture of business	(11,413)	-
Other	133	497
Changes in operating accounts:		
Accounts receivable, net	29,060	14,094
Inventories	(21,191)	(17,822)
Other assets and current assets	(3,099)	599
Accounts payable and accrued liabilities	(9,675)	8,220
Federal and state income taxes	(8,656)	(1,416)
Net cash provided by operating activities	5,682	26,504
Cash flows from investing activities:		
Marketable securities purchased	(109,465)	(27,386)
Marketable securities - maturities and sales	65,250	3,391
Proceeds from divestiture of business, net	64,033	-
Notes issued	-	(2,419)
Purchase of property, plant and equipment	(4,509)	(2,579)
Sale of property, plant and equipment	1	2
Net cash provided by (used in) investing activities	15,310	(28,991)
Cash flows from financing activities:		
Dividends paid	(38,405)	(35,161)
Proceeds from sale of treasury stock	519	443
Other	(114)	-
Net cash used in financing activities	(38,000)	(34,718)
Net decrease in cash and cash equivalents	(17,008)	(37,205)
Cash and cash equivalents at beginning of period	27,034	56,222
Cash and cash equivalents at end of period	\$ 10,026	\$ 19,017

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

NATIONAL PRESTO INDUSTRIES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

NOTE A – BASIS OF PRESENTATION

The consolidated interim financial statements included herein are unaudited and have been prepared by the Company pursuant to the rules and regulations of the United States Securities and Exchange Commission (“SEC”). In the opinion of management of the Company, the consolidated interim financial statements reflect all the adjustments which were of a normal recurring nature necessary for a fair presentation of the results of the interim periods. The condensed consolidated balance sheet as of December 31, 2016 is summarized from audited consolidated financial statements, but does not include all the disclosures contained therein and should be read in conjunction with the 2016 Annual Report on Form 10-K. Interim results for the period are not indicative of those for the year.

On January 3, 2017, the Company and its wholly-owned subsidiary, Presto Absorbent Products, Inc. (“PAPI”), entered into an asset purchase agreement wherein substantially all PAPI assets were sold and certain liabilities were assigned to Drylock Technologies, LTD. (“Drylock”) in exchange for \$68,448,000. The proceeds amount differs from the amount previously disclosed because of the customary post-closing adjustments that were finalized during the second quarter of 2017, totaling \$1,448,000. The asset purchase agreement also provides for additional proceeds of \$4,000,000 upon the sale of certain delayed assets, consisting of machinery and equipment that were the subject of an involuntary conversion, at a future date. As a result of this transaction, effective in the fourth quarter of 2016, the Company classified its results of operations for all periods presented to reflect its Absorbent Products business as a discontinued operation and classified the assets and liabilities of its Absorbent Products business as held for sale. See Note I for further discussion.

NOTE B – RECLASSIFICATIONS

In addition to the reclassifications mentioned in Note A above, certain reclassifications have been made to the prior periods’ financial statements to conform to the current period’s financial statement presentation. These reclassifications did not affect net earnings or stockholders’ equity as previously reported.

NOTE C – EARNINGS PER SHARE

Basic earnings per share is based on the weighted average number of common shares and participating securities outstanding during the period. Diluted earnings per share also includes the dilutive effect of additional potential common shares issuable. Unvested stock awards, which contain non-forfeitable rights to dividends whether paid or unpaid (“participating securities”), are included in the number of shares outstanding for both basic and diluted earnings

per share calculations.

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NOTE D – BUSINESS SEGMENTS

In the following summary, operating profit represents earnings before other income and income taxes. The Company's segments operate discretely from each other with no shared manufacturing facilities. Costs associated with corporate activities (such as cash and marketable securities management) and the assets associated with such activities are included within the Housewares/Small Appliances segment for all periods presented.

	(in thousands)			
	Housewares / Small Appliances	Defense Products	Assets Held for Sale	Total
Quarter ended July 2, 2017				
External net sales	\$ 16,901	\$ 57,660	\$	\$ 74,561
Gross profit	1,528	16,032		17,560
Operating profit (loss)	(949)	13,086		12,137
Total assets	222,165	162,439	5,335	389,939
Depreciation and amortization	308	1,870		2,178
Capital expenditures	463	1,372		1,835
Quarter ended July 3, 2016				
External net sales	\$ 19,280	\$ 50,236	\$	\$ 69,516
Gross profit	3,269	13,898		17,167
Operating profit	699	10,854		11,553
Total assets	161,310	155,032	60,145	376,487
Depreciation and amortization	257	1,776		2,033
Capital expenditures	453	1,090		1,543

	(in thousands)			
	Housewares / Small Appliances	Defense Products	Assets Held for Sale	Total
Six Months ended July 2, 2017				
External net sales	\$ 36,948	\$ 110,467	\$	\$ 147,415
Gross profit	4,697	32,989		37,686
Operating profit (loss)	(402)	26,538		26,136
Total assets	222,165	162,439	5,335	389,939
Depreciation and amortization	611	3,624		4,235
Capital expenditures	923	1,589		2,512

Six Months ended July 3, 2016

External net sales	\$ 40,676	\$ 94,782	\$	\$ 135,458
Gross profit	7,556	25,659		33,215
Operating profit	1,913	19,293		21,206
Total assets	161,310	155,032	60,145	376,487
Depreciation and amortization	498	3,066		3,564
Capital expenditures	892	1,123		2,015

NOTE E - FAIR VALUE OF FINANCIAL INSTRUMENTS

The Company utilizes the methods of fair value as described in Financial Accounting Standard Board (“FASB”) Accounting Standard Codification (“ASC”) 820, Fair Value Measurements and Disclosures, to value its financial assets and liabilities. ASC 820 utilizes a three-tier fair value hierarchy which prioritizes the inputs used in measuring fair value. These tiers include:

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Level 1, defined as observable inputs such as quoted prices in active markets; Level 2, defined as inputs other than quoted prices in active markets that are either directly or indirectly observable; and Level 3, defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions.

The carrying amounts for cash and cash equivalents, accounts receivable, notes receivable, accounts payable, and accrued liabilities approximate fair value due to the immediate or short-term maturity of these financial instruments.

NOTE F - CASH, CASH EQUIVALENTS AND MARKETABLE SECURITIES

The Company considers all highly liquid marketable securities with an original maturity of three months or less to be cash equivalents. Cash equivalents include money market funds. The Company deposits its cash in high quality financial institutions. The balances, at times, may exceed federally insured limits. Money market funds are reported at fair value determined using quoted prices in active markets for identical securities (Level 1, as defined by FASB ASC 820).

The Company has classified all marketable securities as available-for-sale which requires the securities to be reported at estimated fair value, with unrealized gains and losses, net of tax, reported as a separate component of stockholders' equity. Highly liquid, tax-exempt variable rate demand notes with put options exercisable in three months or less are classified as marketable securities.

At July 2, 2017 and December 31, 2016, cost for marketable securities was determined using the specific identification method. A summary of the amortized costs and fair values of the Company's marketable securities at the end of the periods presented is shown in the following table. All of the Company's marketable securities are classified as Level 2, as defined by FASB ASC 820, with fair values determined using significant other observable inputs, which include quoted prices in markets that are not active, quoted prices of similar securities, recently executed transactions, broker quotations, and other inputs that are observable. There were no transfers into or out of Level 2 during the six months ended July 2, 2017.

(In Thousands)				
MARKETABLE SECURITIES				
	Amortized	Fair Value	Gross	Gross
	Cost		Unrealized	Unrealized
			Gains	Losses
July 2, 2017				
Tax-exempt Municipal Bonds	\$ 25,020	\$ 24,983	\$ 9	\$ 46

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Variable Rate Demand Notes	103,723	103,723	-	-
Total Marketable Securities	\$ 128,743	\$ 128,706	\$ 9	\$ 46

December 31, 2016

Tax-exempt Municipal Bonds	\$ 38,223	\$ 38,151	\$ 1	\$ 73
Variable Rate Demand Notes	46,306	46,306	-	-
Total Marketable Securities	\$ 84,529	\$ 84,457	\$ 1	\$ 73

Proceeds from maturities and sales of available-for-sale securities totaled \$38,415,000 and \$2,128,000 for the three month periods ended July 2, 2017 and July 3, 2016, respectively, and totaled \$65,250,000 and \$3,391,000 for the six month periods then ended, respectively. There were no gross gains or losses related to sales of marketable securities during the same periods. Net unrealized gains (losses) included in other comprehensive income were \$(8,000) and \$19,000 before taxes for the three month periods ended July 2, 2017 and July 3, 2016, respectively, and were \$34,000 and \$28,000 before taxes for the six month periods then ended, respectively. No unrealized gains or losses were reclassified out of accumulated other comprehensive income during the same periods.

The contractual maturities of the marketable securities held at July 2, 2017 are as follows: \$20,218,000 within one year; \$16,324,000 beyond one year to five years; \$4,764,000 beyond five years to ten years, and \$87,400,000 beyond ten years. All of the instruments in the beyond five year ranges are variable rate demand notes which can be tendered for cash at par plus interest within seven days. Despite the stated contractual maturity date, to the extent a tender is not honored, the notes become immediately due and payable.

NOTE G – OTHER ASSETS

Other Assets includes prepayments that are made from time to time by the Company for certain materials used in the manufacturing process in the Housewares/Small Appliances segment. The Company expects to utilize the prepayments and related materials over an estimated period of up to three years. As of July 2, 2017 and December 31, 2016, \$14,068,000 and \$10,974,000 of such prepayments, respectively, remained unused and outstanding. At July 2, 2017 and December 31, 2016, \$5,930,000 and \$6,330,000, respectively, of these amounts were included in Other Current Assets, representing the Company's best estimate of the expected utilization of the prepayments and related materials during the twelve-month periods following those dates.

NOTE H – COMMITMENTS AND CONTINGENCIES

The Company is involved in largely routine litigation incidental to its business. Management believes the ultimate outcome of the litigation will not have a material effect on the Company's consolidated financial position, liquidity, or results of operations.

NOTE I – DISCONTINUED OPERATIONS

On January 3, 2017, the Company and its wholly-owned subsidiary, Presto Absorbent Products, Inc. ("PAPI"), entered into an asset purchase agreement wherein substantially all PAPI assets were sold and certain liabilities were assigned to Drylock Technologies, LTD. ("Drylock") in exchange for \$68,448,000. The proceeds amount differs from the amount previously disclosed because of the customary post-closing adjustments that were finalized during the second quarter of 2017, totaling \$1,448,000. The asset purchase agreement also provides for additional proceeds of \$4,000,000 upon the sale of certain delayed assets, consisting of machinery and equipment that were the subject of an involuntary conversion, at a future date. As a result of this transaction, effective in the fourth quarter of 2016, the Company classified its results of operations for all periods presented to reflect its Absorbent Products business as a discontinued operation and classified the assets and liabilities of its Absorbent Products business as held for sale. The Company's pre-tax gain on sale of \$11,413,000, net of one-time transaction costs, was recorded in the first six months of 2017 within earnings from discontinued operations. This amount differs from the gain previously reported as a result of the post-closing adjustments mentioned above that were finalized in the second quarter of 2017.

The following table summarizes the results of the Absorbent Products business within discontinued operations for each of the periods presented:

Three Months Ended Six Months Ended

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(in thousands) (unaudited)	July 2, 2017	July 3, 2016	July 2, 2017	July 3, 2016
Net sales	\$ -	\$ 18,469	\$ 421	\$ 39,024
Cost of sales	(17)	(17,220)	(485)	(36,042)
Selling and general expenses	2	(738)	(24)	(1,414)
Gain on divestiture, net	709	-	11,413	-
Other income	430	(3)	2,078	(3)
Earnings from discontinued operations before provision for income taxes	1,124	508	13,403	1,565
Provision for income taxes from discontinued operations	353	170	4,450	526
Earnings from discontinued operations, net of tax	\$ 771	\$ 338	\$ 8,953	\$ 1,039

The following table summarizes the major classes of assets and liabilities of the Absorbent Products business held for sale for each of the periods presented:

(in thousands)	July 2, 2017 (Unaudited)	December 31, 2016
Accounts receivable, net	\$ 2,351	\$ 13,781
Inventories	-	10,747
Property, plant and equipment, net	2,984	34,365
Assets held for sale	\$ 5,335	\$ 58,893
Accounts payable	\$ 17	\$ 5,245
Accrued liabilities	-	1,008
Liabilities held for sale	\$ 17	\$ 6,253

The Consolidated Statements of Cash Flows do not present the cash flows from discontinued operations separately from cash flows from continuing operations. Cash provided by (used in) operating activities from discontinued operations was \$(5,625,000) and \$2,507,000 for the six months ended July 2, 2017 and July 3, 2016, respectively. Cash provided by (used in) investing activities related to discontinued operations was \$62,036,000 and \$(487,000) for the six months ended July 2, 2017 and July 3, 2016, respectively.

In connection with the asset purchase agreement discussed above, the Company entered into a 10-year lease agreement with Drylock for a portion of its manufacturing and warehouse facilities. The lease agreement provided for total annual payments of \$1,288,000 initially. It also provides Drylock an option for early termination of the lease after the initial five years and an option to modify the space subject to the agreement. Drylock elected the latter option as of June 30, 2017. The agreement allows as well for adjustments to the rental payments based on certain price indices. The Company has also entered into a transition services agreement with Drylock which is expected to continue through the fourth quarter of 2017.

NOTE J – RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In January 2017, the FASB issued ASU No. 2017-04, Intangibles - Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment, which eliminates the performance of Step 2 from the goodwill impairment test. In performing its annual or interim impairment testing, an entity will instead compare the fair value of the reporting unit with its carrying amount and recognize any impairment charge for the amount by which the carrying amount exceeds

the reporting unit's fair value. Additionally, an entity should consider income tax effects from any tax deductible goodwill on the carrying amount of the reporting unit when measuring the goodwill impairment loss. The standard is effective for fiscal years beginning after December 15, 2019. Early adoption is permitted for interim or annual impairment tests performed on testing dates after January 1, 2017. The Company does not expect the adoption of ASU 2017-04 to have a material impact on its consolidated financial statements.

In January 2017, the FASB issued ASU No. 2017-01, Business Combinations (Topic 805): Clarifying the Definition of a Business, which provides guidance in evaluating whether transactions should be accounted for as acquisitions (or disposals) of assets or businesses. The definition of a business affects many areas of accounting, including acquisitions, disposals, goodwill, and consolidation. The guidance is effective for public companies for fiscal years beginning after December 15, 2017, including interim periods within those periods, with early adoption permitted under certain circumstances. The Company does not expect the adoption of ASU 2017-01 to have a material impact on its consolidated financial statements.

In August 2016, the FASB issued ASU No. 2016-15, Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments, which addresses diversity in how certain cash receipts and cash payments are presented and classified in the statement of cash flows. ASU 2016-15 provides guidance on the following eight specific cash flow issues: debt prepayment or debt extinguishment costs; settlement of zero-coupon debt instruments or other debt instruments with coupon interest rates that are insignificant in relation to the effective interest rate of the borrowing; contingent consideration payments made after a business combination; proceeds from the settlement of insurance claims; proceeds from the settlement of corporate-owned life insurance policies, including bank-owned life insurance policies; distributions received from equity

method investees; beneficial interests in securitization transactions; and separately identifiable cash flows and application of the predominance principle. ASU 2016-15 is effective for public business entities for fiscal years beginning after December 15, 2017, and interim periods within those fiscal years. Early adoption is permitted, including adoption in an interim period. The Company does not expect the adoption of ASU 2016-15 to have a material impact on its consolidated financial statements.

In June 2016, the FASB issued ASU No. 2016-13, Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments. ASU 2016-13 provides guidance for estimating credit losses on certain types of financial instruments, including trade receivables, by introducing an approach based on expected losses. The expected loss approach will require entities to incorporate considerations of historical information, current information and reasonable and supportable forecasts. ASU 2016-13 also amends the accounting for credit losses on available-for-sale debt securities and purchased financial assets with credit deterioration. The guidance is effective for fiscal years beginning after December 15, 2019, including interim periods within those fiscal years. The guidance requires a modified retrospective transition method and early adoption is permitted. The Company does not expect the adoption of ASU 2016-13 to have a material impact on its consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, Leases (Topic 842), which establishes a right-of-use (ROU) model that requires a lessee to record a ROU asset and a lease liability on the balance sheet for all leases with terms longer than 12 months. Leases will be classified as either finance or operating, with classification affecting the pattern of expense recognition in the income statement. The new standard is effective for fiscal years beginning after December 15, 2018, including interim periods within those fiscal years. A modified retrospective transition approach is required. The Company is currently evaluating the impact of the adoption of ASU 2016-02 on its consolidated financial statements.

In January 2016, the FASB issued ASU 2016-01, Financial Instruments-Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities, which provides guidance for the recognition, measurement, presentation, and disclosure of financial assets and liabilities. The guidance is effective for reporting periods (interim and annual) beginning after December 15, 2017. The Company does not expect the adoption of ASU 2016-01 to have a material effect on its consolidated financial statements.

In May 2014, the FASB issued ASU 2014-09, Revenue from Contracts with Customers (Topic 606) which amended the existing accounting standards for revenue recognition. ASU 2014-09 establishes principles for recognizing revenue upon the transfer of promised goods or services to customers, in an amount that reflects the expected consideration received in exchange for those goods or services. It is effective for annual reporting periods beginning after December 15, 2017. Early adoption is permitted as of annual reporting periods beginning after December 15, 2016. The amendment may be applied retrospectively to each prior period presented or retrospectively with the cumulative effect recognized as of the date of initial application. The Company expects to adopt ASU 2014-09 as of January 1, 2018, and continues to deliberate on the transition method. While the Company's evaluation of the impact of the standard is ongoing, representative samples of existing revenue contracts have been considered. The Company

continues to evaluate if there will be any effect on the timing and pattern of revenue recognition, and additional disclosures may be required. The Company will continue assessing the impact of ASU 2014-09 on its consolidated financial statements through the date of adoption.

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

Forward-looking statements in this Management's Discussion and Analysis of Financial Condition and Results of Operations, elsewhere in this Form 10-Q, in the Company's 2016 Annual Report to Shareholders, in the Proxy Statement for the annual meeting held on May 16, 2017, and in the Company's press releases and oral statements made with the approval of an authorized executive officer are made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. There are certain important factors that could cause results to differ materially from those anticipated by some of the statements made herein. Investors are cautioned that all forward-looking statements involve risks and uncertainty. In addition to the factors discussed herein and in the Notes to Consolidated Financial Statements, among the other factors that could cause actual results to differ materially are the following: consumer spending and debt levels; interest rates; continuity of relationships with and purchases by major customers; product mix; the benefit and risk of business acquisitions; competitive pressure on sales and pricing; development and market acceptance of new products; increases in material, freight/shipping, or production cost which cannot be recouped in product pricing; delays or interruptions in shipping or production; reliance on third-party suppliers in Asia; shipment of defective product which could result in product liability claims or recalls; work or labor disruptions stemming from a unionized work force; changes in government requirements, military spending, and funding of government contracts, which could result in, among other things, the modification or termination of existing contracts; dependence on subcontractors or vendors to perform as required by contract; the efficient start-up and utilization of capital equipment investments; political actions of federal and state governments which could have an impact on everything from the value of the U.S dollar vis-à-vis other currencies to the availability of affordable labor and energy; and information technology system failures or security breaches. Additional information concerning these and other factors is contained in the Company's Securities and Exchange Commission filings.

Discontinued Operations

On January 3, 2017, the Company and its wholly-owned subsidiary, Presto Absorbent Products, Inc. ("PAPI"), entered into an asset purchase agreement wherein substantially all PAPI assets were sold and certain liabilities were assigned to Drylock Technologies, LTD. As a result of this transaction, effective in the fourth quarter of 2016, the Company classified its results of operations for all periods presented to reflect its Absorbent Products business as a discontinued operation and classified the assets and liabilities of its Absorbent Products business as held for sale. The operations of PAPI previously comprised the Company's Absorbent Products segment.

Comparison of Second Quarter 2017 and 2016

Readers are directed to Note D to the Consolidated Financial Statements, "Business Segments," for data on the financial results of the Company's two business segments for the quarters ended July 2, 2017 and July 3, 2016.

On a consolidated basis, sales increased by \$5,045,000 (7%), gross profit increased by \$393,000 (2%), and selling and general expenses decreased by \$196,000 (4%). Other income increased by \$792,000 (421%), while earnings from continuing operations before provision for income taxes increased by \$1,376,000 (12%), and earnings from continuing operations increased by \$1,005,000 (13%). Earnings from discontinued operations, net of tax, increased \$433,000. Details concerning these changes can be found in the comments by segment below.

Housewares/Small Appliance net sales decreased by \$2,379,000 from \$19,280,000 to \$16,901,000, or 12%, primarily attributable to a decrease in shipments. Defense net sales increased by \$7,424,000 from \$50,236,000 to \$57,660,000, or 15%, primarily reflecting an increase in units shipped.

Housewares/Small Appliance gross profit decreased \$1,741,000 from \$3,269,000 to \$1,528,000, largely reflecting the decrease in sales mentioned above, along with increases in various operating costs that are part of cost of sales. Defense gross profit increased \$2,134,000 from \$13,898,000 to \$16,032,000, primarily reflecting the increase in sales mentioned above.

Selling and general expenses for the Housewares/Small Appliance segment were essentially flat, decreasing \$93,000. Selling and general expenses for the Defense segment decreased \$103,000, primarily reflecting the absence of the prior quarter's non-cash write-down of the book value of equipment of \$353,000, partially offset by increased administrative costs.

The above items were largely responsible for the change in operating profit.

Other income increased \$792,000, approximately a third of which is attributable to interest income, reflecting increased interest rates and funds invested. The balance of the increase is attributable to lease and transition services income mentioned in Note I to the Consolidated Financial Statements.

Earnings from continuing operations before provision for income taxes increased \$1,376,000 from \$11,741,000 to \$13,117,000. The provision for income taxes from continuing operations increased from \$3,805,000 to \$4,176,000, which resulted in an effective income tax rate of 32% for both quarters. Earnings from continuing operations increased \$1,005,000 from \$7,936,000 to \$8,941,000, or 13%.

On January 3, 2017, the Company and its wholly-owned subsidiary, Presto Absorbent Products, Inc. (“PAPI”), entered into an asset purchase agreement wherein substantially all PAPI assets were sold and certain liabilities were assigned to Drylock Technologies, LTD. As a result of this transaction, effective in the fourth quarter of 2016, the Company classified its results of operations for all periods presented to reflect its Absorbent Products business as a discontinued operation and classified the assets and liabilities of its Absorbent Products business as held for sale. Earnings from discontinued operations, net of tax, increased \$433,000, from \$338,000 to \$771,000. The increase was primarily attributable to an expected, customary post-closing adjustment related to the gain on sale mentioned above of \$709,000, before taxes, and a gain on the involuntary conversion of machinery and equipment of \$418,000, before taxes. These were partially offset by the absence of sales and production during the three months ended July 2, 2017.

Net earnings increased \$1,438,000 from \$8,274,000 to \$9,712,000.

Comparison of First Six Months 2017 and 2016

Readers are directed to Note D to the Consolidated Financial Statements, “Business Segments,” for data on the financial results of the Company’s two business segments for the first six months ended July 2, 2017 and July 3, 2016.

On a consolidated basis, sales increased by \$11,957,000 (9%), gross profit increased by \$4,471,000 (14%), selling and general expenses decreased by \$263,000 (2%), and intangibles amortization decreased by \$196,000 (35%). Other income increased by \$1,559,000 (420%), while earnings from continuing operations before provision for income taxes increased by \$6,489,000 (30%), and earnings from continuing operations increased by \$4,468,000 (31%). Earnings from discontinued operations, net of tax, increased \$7,914,000. Details concerning these changes can be found in the comments by segment below.

Housewares/Small Appliance net sales decreased by \$3,728,000 from \$40,676,000 to \$36,948,000, or 9%, approximately 85% of which was attributable to a decrease in shipments, with the remainder attributable to a decrease in prices. Defense net sales increased by \$15,685,000 from \$94,782,000 to \$110,467,000, or 17%, primarily reflecting an increase in units shipped.

Housewares/Small Appliance gross profit decreased \$2,859,000 from \$7,556,000 to \$4,697,000, largely reflecting the decrease in sales mentioned above, along with increases in various operating costs that are part of cost of sales.

Defense gross profit increased \$7,330,000 from \$25,659,000 to \$32,989,000, primarily reflecting the increase in sales mentioned above and an improved product mix.

Selling and general expenses for the Housewares/Small Appliance segment decreased \$544,000, primarily reflecting lower employee benefit cost accruals. Selling and general expenses for the Defense segment increased \$281,000, primarily reflecting increased legal and professional costs of \$360,000. These were largely offset by the absence of the prior period's non-cash write-down of the book value of equipment of \$353,000.

Intangibles amortization decreased by \$196,000. The decrease primarily reflects amortization of the customer contract intangible asset corresponding to the quarter's comparatively lower shipments of a portion of the backlog acquired in late 2013 from DSE, Inc., one of the Company's former competitors in the Defense segment. The DSE asset acquisition is described in Note Q to the Company's 2016 Consolidated Financial Statements on Form 10-K. For the six months ended July 2, 2017 and July 3, 2016, the Company recorded amortization expense of \$361,000 and \$568,000, respectively, associated with the customer contract intangible asset.

The above items were responsible for the change in operating profit.

Other income increased \$1,559,000, approximately a third of which is attributable to interest income, reflecting increased interest rates and funds invested. The balance of the increase is attributable to lease and transition services income mentioned in Note I to the Consolidated Financial Statements.

Earnings from continuing operations before provision for income taxes increased \$6,489,000 from \$21,577,000 to \$28,066,000. The provision for income taxes from continuing operations increased from \$7,131,000 to \$9,152,000, which resulted in an effective income tax rate of 33% for both periods. Earnings from continuing operations increased \$4,468,000 from \$14,446,000 to \$18,914,000, or 31%.

On January 3, 2017, the Company and its wholly-owned subsidiary, Presto Absorbent Products, Inc. ("PAPI"), entered into an asset purchase agreement wherein substantially all PAPI assets were sold and certain liabilities were assigned to Drylock Technologies, LTD. As a result of this transaction, effective in the fourth quarter of 2016, the Company classified its results of operations for all periods presented to reflect its Absorbent Products business as a discontinued operation and classified the assets and liabilities of its Absorbent Products business as held for sale. Earnings from discontinued operations, net of tax, increased \$7,914,000, from \$1,039,000 to \$8,953,000. The increase was primarily attributable to the gain on sale mentioned above of \$11,413,000, before taxes, and a gain on the involuntary conversion of machinery and equipment of \$1,997,000, before taxes. These were partially offset by the absence of sales and production during the remainder of the six month period ended July 2, 2017.

Net earnings increased \$12,382,000 from \$15,485,000 to \$27,867,000.

Liquidity and Capital Resources

Net cash provided by operating activities was \$5,682,000 and \$26,504,000 for the six months ended July 2, 2017 and July 3, 2016, respectively. The principal factors contributing to the decrease can be found in the changes in the components of working capital within the Consolidated Statements of Cash Flows. Of particular note during the first six months of 2017 were net earnings of \$27,867,000, which included total non-cash depreciation and amortization expenses of \$4,284,000, and non-cash gains on the sale of the Absorbent Products business and on an involuntary conversion of machinery and equipment of \$11,413,000 and \$1,997,000, respectively. Contributing to the decrease were increases in inventory levels and deposits made with raw material suppliers included in other assets and current assets, and decreases in payable and accrual levels. These were partially offset by a decrease in accounts receivable levels stemming from cash collections on customer sales. Cash used in operating activities from discontinued operations was \$5,625,000. Of particular note during the first six months of 2016 were net earnings of \$15,485,000, which included total non-cash depreciation and amortization expenses of \$6,465,000, a decrease in accounts receivable levels stemming from cash collections on customer sales, a net increase in payable and accrual levels, and a decrease in deposits made with raw material suppliers included in other assets and current assets. These were partially offset by an increase in inventory levels. Cash provided by operating activities from discontinued operations

was \$2,507,000.

Net cash provided by (used in) investing activities was \$15,310,000 during the first six months of 2017 as compared to \$(28,991,000) during the first six months of 2016. Significant factors contributing to the change in investing cash flows were the proceeds from the 2017 sale of the Absorbent Products business and the issuance of a note receivable during 2016. These were partially offset by increases in net purchases of marketable securities and the acquisition of property, plant, and equipment. Cash provided by (used in) discontinued operations for the first six months of 2017 and 2016 were \$62,036,000 and \$(487,000), respectively.

Cash flows from financing activities for the first six months of 2017 and 2016 primarily differed as a result of the comparative \$0.45 per share increase in the extra dividend paid during the 2017 period. Cash flows for both six-month periods also reflected the proceeds from the sale of treasury stock to a Company sponsored retirement plan.

Working capital decreased by \$19,202,000 during the first six months of 2017 to \$256,939,000 at July 2, 2017 for the reasons stated above. The Company's current ratio was 6.2 to 1.0 at July 2, 2017 and 5.3 to 1.0 at December 31, 2016.

The Company expects to continue to evaluate acquisition opportunities that align with its business segments and will make further acquisitions, as well as continue to make capital investments in these segments per existing authorized projects and for additional projects, if the appropriate return on investment is projected.

The Company has substantial liquidity in the form of cash and cash equivalents and marketable securities to meet all of its anticipated capital requirements, to make dividend payments, and to fund future growth through acquisitions and other means. The bulk of its marketable securities are invested in the tax exempt variable rate demand notes described above and in fixed rate municipal notes and bonds. The Company intends to continue its investment strategy of safety and short-term liquidity throughout its investment holdings.

Critical Accounting Policies

The preparation of the Company's Consolidated Financial Statements in accordance with accounting principles generally accepted in the United States requires management to make certain estimates and assumptions that affect the amount of reported assets and liabilities and disclosure of contingent assets and liabilities at the date of the Consolidated Financial Statements and revenues and expenses during the periods reported. Actual results may differ from those estimates. The Company reviewed the development and selection of the critical accounting policies and believes the following are the most critical accounting policies that could have an effect on the Company's reported results. These critical accounting policies and estimates have been reviewed with the Audit Committee of the Board of Directors.

Inventories

New Housewares/Small Appliance product introductions are an important part of the Company's sales to offset the morbidity rate of other Housewares/Small Appliance products and/or the effect of lowered acceptance of seasonal products due to weather conditions. New products entail unusual risks and have occasionally in the past resulted in losses related to obsolete or excess inventory as a result of low or diminishing demand for a product. There were no such obsolescence issues that had a material effect during the current period, and accordingly, the Company did not record a reserve for obsolete product. In the future should product demand issues arise, the Company may incur losses related to the obsolescence of the related inventory. Inventory risk for the Company's Defense segment is not deemed to be significant, as products are largely built pursuant to customers' specific orders.

Self-Insured Product Liability and Health Insurance

The Company is subject to product liability claims in the normal course of business and is self-insured for health care costs, although it does carry stop loss and other insurance to cover claims once a health care claim reaches a specified threshold. The Company's insurance coverage varies from policy year to policy year, and there are typically limits on all types of insurance coverage, which also vary from policy year to policy year. Accordingly, the Company records an accrual for known claims and incurred but not reported claims, including an estimate for related legal fees in the Company's Consolidated Financial Statements. The Company utilizes historical trends and other analysis to assist in determining the appropriate accrual. There are no known claims that would have a material adverse impact on the Company beyond the reserve levels that have been accrued and recorded on the Company's books and records. An increase in the number or magnitude of claims could have a material impact on the Company's financial condition and

results of operations.

Sales and Returns

Sales are recorded net of discounts and returns for the Housewares/Small Appliance segment. The latter pertain primarily to warranty returns, returns of seasonal items, and returns of those newly introduced products sold with a return privilege. The calculation of warranty returns is based in large part on historical data, while seasonal and new product returns are primarily developed using customer provided information.

Impairment and Valuation of Long-lived Assets

The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the related carrying amounts may not be recoverable. Long-lived assets consist of property, plant and equipment and intangible assets, including the value of a government sales contract. Determining whether an impairment has occurred typically requires various estimates and assumptions, including determining which cash flows are directly related to the potentially impaired asset, the useful life over which cash flows will occur, the amounts of the cash flows and the asset's residual value, if any. In turn, measurement of an impairment loss requires a determination of fair value, which is based on the best information available. The Company uses internal discounted cash flows estimates, quoted market prices when available and independent appraisals, as appropriate, to determine fair value. The Company derives the required cash flow estimates from its historical experience and its internal business plans.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company's interest income on cash equivalents and marketable securities is affected by changes in interest rates in the United States. Cash equivalents primarily consist of money market funds. Based on the accounting profession's interpretation of cash equivalents under FASB ASC Topic 230, the Company's seven-day variable rate demand notes are classified as marketable securities rather than as cash equivalents. The demand notes are highly liquid instruments with interest rates set every seven days that can be tendered to the trustee or remarketer upon seven days notice for payment of principal and accrued interest amounts. The seven-day tender feature of these variable rate demand notes is further supported by an irrevocable letter of credit from highly rated U.S. banks. To the extent a bond is not remarketed at par plus accrued interest, the difference is drawn from the bank's letter of credit. The Company has had no issues tendering these notes to the trustees or remarketers. Other than a failure of a major U.S. bank, there are no risks of which the Company is aware that relate to these notes in the current market. The balance of the Company's investments is held primarily in fixed and variable rate municipal bonds with a weighted average life of 0.7 years. Accordingly, changes in interest rates have not had a material effect on the Company, and the Company does not anticipate that future exposure to interest rate market risk will be material. The Company uses sensitivity analysis to determine its exposure to changes in interest rates.

The Company has no history of, and does not anticipate in the future, investing in derivative financial instruments. Most transactions with international customers are entered into in U.S. dollars, precluding the need for foreign currency cash flow hedges. As the majority of the Housewares/Small Appliance segment's suppliers are located in China, periodic changes in the U.S. dollar and Chinese Renminbi (RMB) exchange rates do have an impact on that segment's product costs. It is anticipated that any potential material impact from fluctuations in the exchange rate will be to the cost of products secured via purchase orders issued subsequent to the revaluation.

ITEM 4. CONTROLS AND PROCEDURES

The Company's management, including the Chief Executive Officer and Chief Financial Officer, have conducted an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures pursuant to Rule 13a-15 under the Securities Exchange Act of 1934 (the "1934 Act") as of July 2, 2017. Based on that evaluation, the Company's Chief Executive Officer and Chief Financial Officer concluded that the Company's disclosure controls and procedures were effective as of that date.

There were no changes to internal controls over financial reporting during the quarter ended July 2, 2017 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

See Note H to the Consolidated Financial Statements set forth under Part I - Item 1 above.

Item 6. Exhibits

- Exhibit 3(i) Restated Articles of Incorporation - incorporated by reference from Exhibit 3 (i) of the Company's annual report on Form 10-K for the year ended December 31, 2005
- Exhibit 3(ii) By-Laws - incorporated by reference from Exhibit 3 (ii) of the Company's current report on Form 8-K dated July 6, 2007
- Exhibit 9.1 Voting Trust Agreement - incorporated by reference from Exhibit 9 of the Company's quarterly report on Form 10-Q for the quarter ended July 6, 1997
- Exhibit 9.2 Voting Trust Agreement Amendment - incorporated by reference from Exhibit 9.2 of the Company's annual report on Form 10-K for the year ended December 31, 2008
- Exhibit 10.1 2017 Incentive Compensation Plan
- Exhibit 10.2 Form of Restricted Stock Award Agreement - 2017 Incentive Compensation Plan
- Exhibit 31.1 Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- Exhibit 31.2 Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- Exhibit 32.1 Certification of the Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- Exhibit 32.2 Certification of the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- Exhibit 101 The following financial information from National Presto Industries, Inc.'s Quarterly Report on Form 10-Q for the period ended July 2, 2017, formatted in eXtensible Business Reporting Language (XBRL):
 - (i) Condensed Consolidated Balance Sheets, (ii) Consolidated Statements of Comprehensive Income, (iii) Consolidated Statements of Cash Flows, and (iv) Notes to Consolidated Financial Statements.

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.

NATIONAL PRESTO INDUSTRIES, INC.

/s/ Maryjo Cohen
Maryjo Cohen, Chair of the Board,
President, Chief Executive Officer
(Principal Executive Officer), Director

/s/ Randy F. Lieble
Randy F. Lieble, Director, Vice President,
Chief Financial Officer (Principal
Financial Officer), Treasurer

Date: August 11, 2017

National Presto Industries, Inc.

Exhibit Index

Exhibit Number	Exhibit Description
10.1	2017 Incentive Compensation Plan
10.2	Form of Restricted Stock Award Agreement – 2017 Incentive Compensation Plan
31.1	Chief Executive Officer Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Chief Financial Officer Certification pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Chief Executive Officer Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Chief Financial Officer Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
101	The following financial information from National Presto Industries, Inc.'s Quarterly Report on Form 10-Q for the period ended July 2, 2017, formatted in eXtensible Business Reporting Language (XBRL): (i) Condensed Consolidated Balance Sheets, (ii) Consolidated Statements of Comprehensive Income, (iii) Consolidated Statements of Cash Flows, and (iv) Notes to Consolidated Financial Statements.