AXT INC
Form 10-Q
May 09, 2014

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

FORM 10-Q

(Mark One)

x Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

for the quarterly period ended March 31, 2014

Or

o Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

for the transition period from to

Commission File Number 000-24085

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

DELAWARE	94-3031310
(State or other jurisdiction of Incorporation or organization)	(I.R.S. Employer Identification No.)

4281 Technology Drive, Fremont, California 94538
(Address of principal executive offices) (Zip code)

(510) 683-5900
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities 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 x No o

Indicate by check mark whether the registrant has submitted electronically and posted on its Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

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

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

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

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

Class	Outstanding at May 5, 2014
Common Stock, $0.001 par value	32,604,958

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements (Unaudited)

AXT, INC.
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited, in thousands, except per share data)

	March 31, 2014	December 31, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	$22,760	$24,961
Short-term investments	22,375	12,499
Accounts receivable, net of allowances of $791 and $1,054 as of March 31, 2014 and December 31, 2013	16,364	14,943
Inventories	38,040	39,127
Prepaid expenses and other current assets	6,401	8,010
Total current assets	105,940	99,540
Long-term investments	1,678	10,145
Property, plant and equipment, net	36,179	37,621
Related party notes receivable – long-term	1,701	1,715
Other assets	14,752	14,801
Total assets	$160,250	$163,822
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Accounts payable	$7,618	$8,140
Accrued liabilities	6,646	7,286
Total current liabilities	14,264	15,426
Long-term portion of royalty payments	2,325	2,525
Other long-term liabilities	272	325
Total liabilities	16,861	18,276
Commitments and contingencies (Note 11)		
Stockholders' equity:		
Preferred stock, $0.001 par value; 2,000 shares authorized; 883 shares issued and outstanding as of March 31, 2014 and December 31, 2013 (Liquidation preference of $6.2 million and $6.1 million as of March 31, 2014 and December 31, 2013, respectively)	3,532	3,532
Common stock, $0.001 par value per share; 70,000 shares authorized; 32,605 and 32,605 shares issued and outstanding as of March 31, 2014 and December 31, 2013, respectively	32	32
Additional paid-in capital	194,448	194,156
Accumulated deficit	(69,045)	(67,005)
Accumulated other comprehensive income	8,500	8,953
AXT, Inc. stockholders' equity	137,467	139,668
Noncontrolling interests	5,922	5,878
Total stockholders' equity	143,389	145,546
Total liabilities and stockholders' equity	$160,250	$163,822

See accompanying notes to condensed consolidated financial statements.

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AXT, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited, in thousands, except per share data)

	Three Months Ended March 31, 2014	2013
Revenue	$19,345	$22,380
Cost of revenue	16,627	18,896
Gross profit	2,718	3,484
Operating expenses:		
Selling, general and administrative	3,436	3,925
Research and development	775	822
Restructuring charge	907	—
Total operating expenses	5,118	4,747
Loss from operations	(2,400)	(1,263)
Interest income, net	127	31
Equity in earnings of unconsolidated joint ventures	487	282
Other income (expense), net	10	(825)
Loss before provision for income taxes	(1,776)	(1,775)
Provision (benefit) for income taxes	59	184
Net loss	(1,835)	(1,959)
Less: Net loss attributable to noncontrolling interests	(205)	(441)
Net loss attributable to AXT, Inc.	$(2,040)	$(2,400)
Net loss attributable to AXT, Inc. per common share:		
Basic	$(0.06)	$(0.08)
Diluted	$(0.06)	$(0.08)
Weighted average number of common shares outstanding:		
Basic	32,364	32,297
Diluted	32,364	32,297

See accompanying notes to condensed consolidated financial statements.

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AXT, INC.
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)
(Unaudited, in thousands)

	Three Months Ended March 31, 2014	2013
Net income (loss)	$(1,835)	$(1,959)
Other comprehensive income (loss), net of tax:		
Change in foreign currency translation gain (loss), net of tax	(521)	407
Change in unrealized gain (loss) on available-for-sale investments, net of tax	(10)	(17)
Total other comprehensive income, net of tax	(531)	390
Comprehensive income (loss)	(2,366)	(1,569)
Less: Comprehensive income attributable to the noncontrolling interests	(126)	(498)
Comprehensive income (loss) attributable to AXT, Inc.	$(2,492)	$(2,067)

See accompanying notes to condensed consolidated financial statements.

AXT, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited, in thousands)

	Three Months Ended March 31,	
	2014	2013
Cash flows from operating activities:		
Net Loss	$(1,835)	$(1,959)
Adjustments to reconcile net loss to net cash from operating activities:		
Depreciation and amortization	1,404	1,291
Amortization of marketable securities premium	122	146
Stock-based compensation	292	332
Loss (gain) on disposal of property, plant and equipment	(5)	—
Provision for doubtful accounts	1	—
Changes in assets and liabilities:		
Accounts receivable, net	(1,459)	922
Inventories	985	1,649
Prepaid expenses and other current assets	1,584	(1,740)
Other assets	18	105
Accounts payable	(489)	664
Accrued liabilities	(697)*	(164)*
Other long-term liabilities	(308)	(270)
Net cash (used in) provided by operating activities	(387)	976
Cash flows from investing activities:		
Purchases of property, plant and equipment	(163)	(1,349)
Proceeds from sales of property, plan and equipment	5	—
Purchases of available-for-sale securities	(3,725)	(12,410)
Proceeds from maturities of available-for-sale securities	2,180	8,130
Net cash used in investing activities	(1,703)	(5,629)
Cash flows from financing activities:		
Proceeds from common stock options exercised	—	256
Dividends paid by joint ventures	—	(532)
Net cash used in financing activities	—	(276)
Effect of exchange rate changes on cash and cash equivalents	(111)	87
Net decrease in cash and cash equivalents	(2,201)	(4,842)
Cash and cash equivalents at the beginning of the period	24,961	30,634
Cash and cash equivalents at the end of the period	$22,760	$25,792

* Dividends accrued but not paid by joint ventures of $729 and $2,365 was included in accrued liabilities as of March 31, 2014 and March 31, 2013, respectively.

See accompanying notes to condensed consolidated financial statements.

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AXT, INC.
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

Note 1. Basis of Presentation

The accompanying condensed consolidated financial statements of AXT, Inc. (“AXT,” the “Company,” “we,” “us,” and “our” refer to AXT, Inc. and all of its consolidated subsidiaries) are unaudited, and have been prepared in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, the year-end condensed consolidated balance sheet data was derived from our audited consolidated financial statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America. In the opinion of our management, the unaudited condensed consolidated financial statements reflect all adjustments, consisting only of normal recurring adjustments, considered necessary to present fairly the financial position, results of operations and cash flows of AXT and our consolidated subsidiaries for all periods presented.

Our management has made a number of estimates and assumptions relating to the reporting of assets and liabilities and the disclosure of contingent assets and liabilities to prepare these condensed consolidated financial statements in conformity with accounting principles generally accepted in the United States of America. Actual results could differ materially from those estimates.

The results of operations are not necessarily indicative of the results to be expected in the future or for the full fiscal year. It is recommended that these condensed consolidated financial statements be read in conjunction with our consolidated financial statements and the notes thereto included in our 2013 Annual Report on Form 10-K filed with the Securities and Exchange Commission (the “SEC”) on March 14, 2014.

The consolidated financial statements include the accounts of AXT, our wholly-owned subsidiary, Beijing Tongmei Xtal Technology Co, Ltd. and our majority owned subsidiaries, Beijing JiYa Semiconductor Material Co., Ltd., Nanjing Jin Mei Gallium Co., Ltd. and Beijing BoYu Semiconductor Vessel Craftwork Technology Co., Ltd. All significant inter company accounts and transactions have been eliminated. Investments in business entities in which we do not have control, but have the ability to exercise significant influence over operating and financial policies (generally 20-50% ownership), are accounted for by the equity method. For majority-owned subsidiaries, we reflect the noncontrolling interest of the portion we do not own on our condensed consolidated balance sheets in stockholders’ equity and in our condensed consolidated statements of operations.

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Note 2. Investments and Fair Value Measurements

Our cash, cash equivalents and investments are classified as follows (in thousands):

	March 31, 2014				December 31, 2013			
	Amortized Cost	Gross Unrealized Gain	Gross Unrealized (Loss)	Fair Value	Amortized Cost	Gross Unrealized Gain	Gross Unrealized (Loss)	Fair Value
Classified as:								
Cash	$21,638	$ —	$ —	$21,638	$24,852	$ —	$ —	$24,852
Cash equivalents:								
Money market fund	1,122	—	—	1,122	109	—	—	109
Total cash and cash equivalents	22,760	—	—	22,760	24,961	—	—	24,961
Investments (available for sale):								
Certificates of deposit	7,864	1	(2)	7,863	6,320	2	(4)	6,318
Corporate bonds	14,155	12	(2)	14,165	14,276	8	(6)	14,278
Corporate equity security	125	1,900	—	2,025	125	1.923	—	2,048
Total investments	22,144	1,913	(4)	24,053	20,721	1,933	(10)	22,644
Total cash, cash equivalents and investments	$44,904	$ 1,913	$ (4)	$46,813	$45,682	$ 1,933	$ (10)	$47,605
Contractual maturities on investments:								
Due within 1 year	$20,464			$22,375	$10,569			$12,499
Due after 1 through 5 years	1,680			1,678	10,152			10,145
	$22,144			$24,053	$20,721			$22,644

We manage our investments as a single portfolio of highly marketable securities that is intended to be available to meet our current cash requirements. We have no investments in auction rate securities. There were no sales of available-for-sales securities and no realized gains and losses for the three months ended March 31, 2014 and 2013.

Also included in short-term investments at March 31, 2014 is our investment in the common stock of Intelligent Epitaxy Technology, Inc (IntelliEPI), a Taiwan publicly-traded company. We began classifying this asset as an available-for- sale security upon its initial public offering (IPO) in 2013. Prior to the IPO in 2013, we sold some of our stock in IntelliEPI and realized a gain of approximately $800,000. An unrealized gain of $1.6 million net of tax was recorded as of March 31, 2014. These securities are valued at fair market value at March 31, 2014. There is no assurance that the Company will realize this value when the securities are sold in the future.

The gross unrealized losses related to our portfolio of available-for-sale securities were primarily due to changes in interest rates and market and credit conditions of the underlying securities. We have determined that the gross unrealized losses on some of our available-for-sale securities as of March 31, 2014 are temporary in nature. We periodically review our investment portfolio to identify and evaluate investments that have indications of possible impairment. Factors considered in determining whether a loss is temporary include the magnitude of the decline in market value, the length of time the market value has been below cost (or adjusted cost), credit quality, and our ability and intent to hold the securities for a period of time sufficient to allow for any anticipated recovery in market value.

The following table summarizes the fair value and gross unrealized losses related to available-for-sale securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position as of March 31, 2014 (in thousands):

	In Loss Position < 12 months		In Loss Position > 12 months		Total In Loss Position	
	Fair Value	Gross Unrealized (Loss)	Fair Value	Gross Unrealized (Loss)	Fair Value	Gross Unrealized (Loss)
Investments:						
Certificates of deposit	$1,918	$ (1)	$1,239	$ (1)	$3,157	$ (2)
Corporate bonds	—	—	2,382	(2)	2,382	(2)
Total in loss position	$1,918	$ (1)	$3,621	$ (3)	$5,539	$ (4)

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The following table summarizes the fair value and gross unrealized losses related to available-for-sale securities, aggregated by investment category and length of time that individual securities have been in a continuous unrealized loss position as of December 31, 2013 (in thousands):

	In Loss Position < 12 months		In Loss Position > 12 months		Total In Loss Position	
	Fair Value	Gross Unrealized (Loss)	Fair Value	Gross Unrealized (Loss)	Fair Value	Gross Unrealized (Loss)
Investments:						
Certificates of deposit	$3,425	$ (4)	$720	$ (0)	$4,145	$ (4)
Corporate bonds	4,473	(5)	3,711	(1)	8,184	(6)
Total in loss position	$7,898	$ (9)	$4,431	$ (1)	$12,329	$ (10)

Investments in Privately-held Companies

We have made strategic investments in private companies located in China in order to gain access at a competitive cost to raw materials that are critical to our substrate business (see Note 6). The investment balances for all of these companies, including minority investments indirectly in privately-held companies made by our consolidated joint ventures, accounted for under the equity method are included in “other assets” in the consolidated balance sheets and totaled $11.0 million and $10.9 million as of March 31, 2014 and December 31, 2013, respectively.

We also maintain minority investments in one company which is accounted for under the cost method as we do not have the ability to exercise significant influence over their operations. Our investments under the cost method are reviewed for other than temporary declines in value on a quarterly basis. We monitor our investments for impairment and record reductions in carrying value when events or changes in circumstances indicate that the carrying value may not be recoverable. As of March 31, 2014 and December 31, 2013, our investments in this unconsolidated company had a carrying value of $200,000 and were also included in “other assets” in the condensed consolidated balance sheets.

Fair Value Measurements

ASC topic 820, Fair value measurement (“ASC 820”) establishes three levels of inputs that may be used to measure fair value. Level 1 instrument valuations are obtained from real-time quotes for transactions in active exchange markets involving identical assets. Level 2 instrument valuations are obtained from readily-available pricing sources for comparable instruments. Level 3 instrument valuations are obtained from unobservable inputs in which there is little or no market data, which require us to develop our own assumptions. As of March 31, 2014, we did not have any Level 3 assets or liabilities. On a recurring basis, we measure certain financial assets and liabilities at fair value, primarily consisting of our short-term and long-term investments.

The type of instrument valued based on quoted market prices in active markets include our money market funds, which are generally classified within Level 1 of the fair value hierarchy. Other than corporate equity securities which are based on quoted market prices and classified as Level 1, we classify our available-for-sale securities including certificates of deposit, corporate bonds as having Level 2 inputs. The valuation techniques used to measure the fair value of these financial instruments having Level 2 inputs were derived from quoted market prices, broker or dealer quotations, or alternative pricing sources with reasonable levels of price transparency. There were no changes in valuation techniques or related inputs in the three months ended March 31, 2014. There have been no transfers between fair value measurement levels during the three months ended March 31, 2014.

The following table summarizes our financial assets and liabilities measured at fair value on a recurring basis in accordance with ASC 820 as of March 31, 2014 (in thousands):

	Balance as of March 31, 2014	Quoted Prices in Active Markets of Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)
Assets:			
Cash equivalents and investments:			
Money market fund	$1,122	$ 1,122	$ —
Certificates of deposit	7,863	—	7,863
Corporate bonds	14,165	—	14,165
Corporate equity securities	2,025	2,025	—
Total	$25,175	$ 3,147	$ 22,028
Liabilities	$—	$ —	$ —

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The following table summarizes our financial assets and liabilities measured at fair value on a recurring basis in accordance with ASC 820 as of December 31, 2013 (in thousands):

	Balance as of December 31, 2013	Quoted Prices in Active Markets of Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)
Assets:			
Cash equivalents and investments:			
Money market fund	$ 109	$ 109	$ —
Certificates of deposit	6,318	—	6,318
Corporate bonds	14,278	—	14,278
Corporate equity securities	2,048	2,048	—
Total	$ 22,753	$ 2,157	$ 20,596
Liabilities	$ —	$ —	$ —

Items Measured at Fair Value on a Nonrecurring Basis

Certain assets that are subject to nonrecurring fair value measurements are not included in the table above. These assets include investments in privately-held companies accounted for by equity and cost method (See Note 6). We did not record other-than-temporary impairment charges for either of these investments during the three months ended March 31, 2014 or 2013.

Note 3. Inventories

The components of inventories are summarized below (in thousands):

	March 31, 2014	December 31, 2013
Inventories:		
Raw materials	$ 19,873	$ 21,063
Work in process	14,396	14,027
Finished goods	3,771	4,037
	$ 38,040	$ 39,127

As of March 31, 2014 and December 31, 2013, carrying values of inventories were net of inventory reserve of $11.5 million and $11.0 million, respectively, for excess and obsolete inventory.

Note 4. Accrued Liabilities

The components of accrued liabilities are summarized below (in thousands):

	March 31,	December 31,

	2014	2013
Accrued product warranty	$1,227	$ 1,048
Accrued compensation and related charges	1,210	1,762
Current portion of royalty payments	800	800
Dividends payable by consolidated joint ventures	729	649
Accrued professional services	279	543
Accrued income taxes	100	125
Other accrued liabilities	2,301	2,359
	$6,646	$ 7,286

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Note 5. Related Party Transactions

In August 2011, our consolidated joint venture, Beijing JiYa Semiconductor Material Co., Ltd. (JiYa), entered into a non-interest bearing note agreement in the amount of $1.7 million (Rmb 10,485,200) with one of its equity investment entities The original term of the loan was for two years and ten months with 3 periodic principal payments required. After various amendments to the terms of the note, in December 2013 the parties agreed to delay all principal repayment until December 2016. As of March 31, 2014, and December 31, 2013, we included $1.7 million (Rmb 10,485,200) in “Related party notes receivable – long term” in our consolidated balance sheets.

Beginning in 2012, JiYa is contractually obligated under an agency sales agreement to sell raw material on behalf of one of its equity investment entities. Jiya bills the customers and remits the receipts, net of its portions of sales commission, to this equity investment entity. For the three months ended March 31, 2014 and 2013, JiYa has recorded $0 and $10,000 of income from agency sales respectively, which was included in “other expense, net” in our condensed consolidated statements of operations. As of March 31, 2014 and December 31, 2013, there were no amounts payable to this equity investment entity.

JiYa also purchases raw materials from one of its equity investment entities for production in the ordinary course of business. As of March 31, 2014 and December 31, 2013, amounts payable of $1.2 million and $1.5 million, respectively, were included in “accounts payable” in our condensed consolidated balance sheets.

Beginning in 2012, our consolidated joint venture, Nanjing Jin Mei Gallium Co., Ltd (Jin Mei) is contractually obligated under an agency sales agreement to sell raw material on behalf of its equity investment entity. Jin Mei bills the customers and remits the receipts, net of its portions of sales commission, to this equity investment entity. For the three months ended March 31, 2014 and 2013, Jin Mei has recorded $5,000 and $65,000 income from agency sales, respectively, which were included in “other income (expense), net” in the consolidated statements of operations.

In March 2012, our wholly-owned subsidiary, Beijing Tongmei Xtal Technology Co., Ltd. (Tongmei), entered into an operating lease for the land it owns with our consolidated joint venture Beijing BoYu Semiconductor Vessel Craftwork Technology Co., Ltd. The lease agreement for the land of approximately 22,081 square feet commenced on January 1, 2012 for a term of 10 years with annual lease payments of $24,000 (Rmb 150,000) subject to a 5% increase at each third year anniversary. The annual lease payment is due by January 31 of each year.

Tongmei has paid $120,000 (Rmb 740,924) on behalf of Donghai County Dongfang High Purity Electronic Materials Co., Ltd. its equity investment entity, to purchase materials. As of March 31, 2014, this balance was included in "prepaid expenses and other current assets" in our consolidated balance sheets.

Our Related Party Transactions Policy seeks to prohibit all conflicts of interest in transactions between related parties and us, unless they have been approved by our Board of Directors. This policy applies to all of our employees and directors, our subsidiaries and our joint ventures. Our executive officers retain board seats on the board of directors of the companies in which we have invested in our China joint ventures. See Note 6 for further details.

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Note 6. Investments in Privately-held Companies

We have made strategic investments in private companies located in China in order to gain access at a competitive cost to raw materials that are critical to our substrate business.

Our investments are summarized below (in thousands):

Company	Investment Balance as of March 31, 2014	Investment Balance as of December 31, 2013	Accounting Method	Ownership Percentage
Beijing JiYa Semiconductor Material Co., Ltd.	$3,331	$ 3,331	Consolidated	46 %
Nanjing Jin Mei Gallium Co., Ltd.	592	592	Consolidated	83 %
Beijing BoYu Semiconductor Vessel Craftwork Technology Co., Ltd.	1,346	1,346	Consolidated	70 %
	$5,269	$ 5,269		
Donghai County Dongfang High Purity Electronic Materials Co., Ltd.	$1,867	$ 1,900	Equity	46 %
Xilingol Tongli Germanium Co. Ltd.	4,849	4,692	Equity	25 %
Emeishan Jia Mei High Purity Metals Co., Ltd.	925	945	Equity	25 %
	$7,641	$ 7,537		

Our ownership of Beijing JiYa Semiconductor Material Co., Ltd. (JiYa) is 46%. We continue to consolidate JiYa as we have significant influence in management and have majority control of the board. Our Chief Executive Officer is chairman of the JiYa board, while our president of China operations, our vice president of China administration and our vice president of wafer production are also members of the board.

Our ownership of Nanjing Jin Mei Gallium Co., Ltd. (Jin Mei) is 83%. We continue to consolidate Jin Mei as we have significant influence in management and have majority control of the board. Our Chief Executive Officer is chairman of the Jin Mei board, while our president of China operations and our vice president of China administration are also members of the board.

Our ownership of Beijing BoYu Semiconductor Vessel Craftwork Technology Co., Ltd. (BoYu) is 70%. We continue to consolidate BoYu as we have a significant influence in management and have majority control of the board. Our Chief Executive Officer is chairman of the BoYu board, while our president of China operations and our vice president of China administration are also members of the board.

Although we have representation on the boards of directors of each of these companies, the daily operations of each of these companies are managed by local management and not by us. Decisions concerning their respective short term strategy and operations, any capacity expansion and annual capital expenditures, and decisions concerning sales of finished product, are made by local management with some inputs from us.

During the three months ended March 31, 2014 and 2013, the three consolidated joint ventures generated $0.8 million and $1.3 million of income, respectively, of which $205,000 and $441,000, respectively, were allocated to minority interests, resulting in $548,000 and $852,000 of income, respectively, to our net income (loss).

For the three minority investment entities that are not consolidated, the investment balances are included in “other assets” in our condensed consolidated balance sheets and totaled $7.6 million and $7.5 million as of March 31, 2014 and December 31, 2013. We own 46% of the ownership interests in one of these companies and 25% in each of the other two companies. These three companies are not considered variable interest entities because:

- all three companies have sustainable businesses of their own;
- our voting power is proportionate to our ownership interests;
- we only recognize our respective share of the losses and/or residual returns generated by the companies if they occur; and
- we do not have controlling financial interest in, do not maintain operational or management control of, do not control the board of directors of, and are not required to provide additional investment or financial support to any of these companies.

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We also maintain minority investments in privately-held companies made indirectly through our consolidated joint ventures. These minority investments are accounted for under the equity method in the books of our consolidated joint ventures. As of March 31, 2014 and December 31, 2013, our consolidated joint ventures included these minority investments in "other assets" in the condensed consolidated balance sheets with a carrying value of $3.4 million.

All of the minority investment entities that are not consolidated and accounted for under the equity method had the following summarized income information (in thousands) for the three months ended March 31, 2014 and 2013.

	Three Months Ended March 31, 2014	2013
Net Sales	$13,480	$9,273
Gross profit	3,963	3,124
Operating income	2,664	1,614
Net income	2,119	1,295

Our gross entity earnings from all the minority investment entities that are not consolidated and accounted for under the equity method were $487,000 and $282,000 for the three months ended March 31, 2014 and 2013, respectively.

We also maintain minority investments directly in one privately-held companies accounted for under the cost method and we do not have the ability to exercise significant influence over their operations. As of March 31, 2014 and December 31, 2013, our investments in this unconsolidated privately-held company had a carrying value of $200,000 and are included in "other assets" in the condensed consolidated balance sheets.

Note 7. Stockholders' Equity and Stock Repurchase Program

Consolidated Statements of Changes in Equity

	Preferred Stock	Common Stock	Additional Paid In Capital	Accumulated Deficit	Other Comprehensive Income/(loss)	AXT, Inc. stockholders' equity	Noncontrolling interests	Total stockholders' equity
Balance as of December 31, 2013	$3,532	$ 32	$194,156	$(67,005)	$ 8,953	$139,668	$ 5,878	$145,546
Stock-based compensation			292			292		292
Net (loss) income				(2,040)		(2,040)	205	(1,835)
Dividends declared by joint ventures							(83)	(83)
Change in unrealized (loss) gain on marketable securities					(10)	(10)		(10)
Currency translation adjustment					(442)	(442)	(79)	(521)
Balance as of March 31, 2014	$3,532	$ 32	$194,448	$(69,045)	$ 8,501	$137,468	$ 5,921	$143,389

There were no reclassification adjustments from accumulated other comprehensive income for the three months ended March 31, 2014 and March 31, 2013.

Stock Repurchase Program

On February 21, 2013, our Board of Directors approved a stock repurchase program pursuant to which we may repurchase up to $6.0 million of our outstanding common stock through February 27, 2014. These purchases can be made from time to time in the open market and are funded from our existing cash balances and cash generated from operations. During 2013, we repurchased approximately 285,000 shares at an average price of $2.51 per share for a total purchase price of $716,000 under the stock repurchase program.

As of December 31, 2013, approximately $5.3 million remained available for future repurchases under this program. No shares were repurchased in the three months ended March 31, 2014 under this program. This repurchase plan expired on February 27, 2014. See Item 2, Unregistered Sales of Equity Securities and Use of Proceeds in Part II, Other Information, for additional information.

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Note 8. Stock-Based Compensation

We account for stock-based compensation in accordance with the provisions of FASB Accounting Standards Codification (“ASC”) topic 718, Compensation-Stock Compensation (“ASC 718”), which established accounting for stock-based awards exchanged for employee services. Stock-based compensation cost is measured at each grant date, based on the fair value of the award, and is recognized as expense over the employee’s requisite service period of the award. All of our stock compensation is accounted for as an equity instrument.

The following table summarizes compensation costs related to our stock-based awards (in thousands, except per share data):

	Three Months Ended March 31,	
	2014	2013
Cost of revenue	$5	$6
Selling, general and administrative	244	284
Research and development	43	42
Total stock-based compensation	292	332
Tax effect on stock-based compensation	—	—
Net effect on net income (loss)	$292	$332

As of March 31, 2014, the unamortized compensation costs related to unvested stock options granted to employees under our stock option plans were approximately $1.4 million, net of estimated forfeitures of $92,000. These costs are amortized on a straight-line basis over a weighted-average period of approximately 2.6 years and will be adjusted for subsequent changes in estimated forfeitures. We elected not to capitalize any stock-based compensation to inventory as of March 31, 2014 due to the immateriality of the amount.

We estimate the fair value of stock options using a Black-Scholes valuation model, consistent with the provisions of ASC 718. There were no stock options granted in the three months ended March 31, 2014 and 2013.

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The following table summarizes our stock option activities during the three months ended March 31, 2014 (in thousands, except per share data):

Stock Options	Shares	Weighted-average Exercise Price	Weighted-average Remaining Contractual Life (in years)	Aggregate Intrinsic Value
Balance as of January 1, 2014	2,671	$ 3.29	6.71	$ 893
Granted	—	—		
Exercised	—	—		
Canceled and expired	(74)	5.18		
Balance as of March 31, 2014	2,597	$ 3.24	6.65	$ 438
Options vested and expected to vest as of March 31, 2014	2,597	$ 3.24	6.65	$ 438
Options exercisable as of March 31, 2014	1,663	$ 3.30	5.43	$ 438

The aggregate intrinsic value in the table above represents the total pretax intrinsic value, based on our closing price of $2.20 on March 31, 2014, which would have been received by the option holder had all option holders exercised their options on that date.

Restricted stock awards

A summary of activity related to restricted stock awards for the three months ended March 31, 2014 is presented below:

Stock Awards	Shares	Weighted-Average Grant Date Fair Value
Non-vested as of January 1, 2014	241,232	$ 3.44
Granted	—	$ —
Vested	—	$ —
Non-vested as of March 31, 2014	241,232	$ 3.44

As of March 31, 2014, the unamortized compensation costs related to unvested restricted stock awards was approximately $581,000, which is to be amortized on a straight-line basis over a weighted average period of approximately 2.3 years.

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Note 9. Net Income (loss) Per Share

Basic net income (loss) per share is computed using the weighted-average number of common shares outstanding during the periods less shares of common stock subject to repurchase and non-vested stock awards. Diluted net income (loss) per share is computed using the weighted-average number of common shares outstanding and potentially dilutive common shares outstanding during the periods. The dilutive effect of outstanding stock options and restricted stock awards is reflected in diluted earnings per share by application of the treasury stock method. Potentially dilutive common shares consist of common shares issuable upon the exercise of stock options. Potentially dilutive common shares are excluded in net loss periods, as their effect would be anti-dilutive.

A reconciliation of the numerators and denominators of the basic and diluted net loss per share calculations is as follows (in thousands, except per share data):

	Three Months Ended March 31,	
	2014	2013
Numerator:		
Net loss attributable to AXT, Inc.	$(2,040)	$(2,400)
Less: Preferred stock dividends	(44)	(44)
Net loss available to common stockholders	$(2,084)	$(2,444)
Denominator:		
Denominator for basic net loss per share - weighted average common shares	32,364	32,297
Effect of dilutive securities:		
Common stock options	—	—
Restricted stock awards	—	—
Denominator for dilutive net loss per common share	32,364	32,297
Net loss attributable to AXT, Inc. per common share:		
Basic	$(0.06)	$(0.08)
Diluted	$(0.06)	$(0.08)
Weighted-average shares:		
Options excluded from diluted net loss per share as the impact is anti-dilutive	2,607	2,656
Restricted stock excluded from diluted net loss per share as the impact is anti-dilutive	241	239

The 883,000 shares of $0.001 par value Series A preferred stock issued and outstanding as of March 31, 2014 and December 31, 2013, valued at $3,532,000, are non-voting and non-convertible preferred stock with a 5.0% cumulative annual dividend rate payable when declared by the board of directors and a $4 per share liquidation preference over common stock, which must be paid before any distribution is made to common stockholders. These preferred shares were issued to Lyte Optronics, Inc. stockholders in connection with the completion of our acquisition of Lyte Optronics, Inc. on May 28, 1999.

Note 10. Segment Information and Foreign Operations

Segment Information

We operate in one segment for the design, development, manufacture and distribution of high-performance compound semiconductor substrates and sale of materials. In accordance with ASC topic 280, Segment Reporting, our chief operating decision-maker has been identified as our Chief Executive Officer, who reviews operating results to make decisions about allocating resources and assessing performance for the Company. Since we operate in one segment, all financial segment and product line information can be found in our condensed consolidated financial statements.

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The following table represents revenue amounts (in thousands) by product type:

	Three Months Ended March 31, 2014	2013
Product type:		
GaAs substrates	$8,488	$11,723
InP substrates	2,180	1,849
Ge substrates	3,278	2,551
Raw materials and other	5,399	6,257
Total	$19,345	$22,380

The following table represents revenue amounts (in thousands) reported for products shipped to customers in the corresponding geographic region:

	Three Months Ended March 31, 2014	2013
Geographical information:		
Europe (primarily Germany)	$6,583	$4,689
China	4,165	6,029
Asia Pacific (excluding China, Japan and Taiwan)	2,389	2,132
Taiwan	2,115	3,779
Japan	2,313	2,282
North America (primarily the United States)	1,780	3,469
Total	$19,345	$22,380

Long-lived assets consist primarily of property, plant and equipment, and are attributed to the geographic location in which they are located. Long-lived assets by geographic region were as follows (in thousands):

	As of March 31, 2014	December 31, 2013
Long-lived assets by geographic region:		
North America	$179	$ 204
China	36,000	37,417
	$36,179	$ 37,621

Significant Customers

No customer represented more than 10% of our revenue for the three months ended March 31, 2014 and 2013. Our top five customers, although not the same five customers for each period, represented 39% and 34% of our revenue for the three months ended March 31, 2014 and 2013, respectively.

We perform ongoing credit evaluations of our customers' financial condition, and limit the amount of credit extended when deemed necessary, but generally do not require collateral. No customer accounted for over 10% of our trade accounts receivable balance as of March 31, 2014 while one customer accounted for 20% of our trade accounts receivable balance as of December 31, 2013.

Note 11. Commitments and Contingencies

Indemnification Agreements

We enter into standard indemnification arrangements with our customers in the ordinary course of business. Pursuant to these arrangements, we indemnify, hold harmless, and agree to reimburse the indemnified parties for losses suffered or incurred by the indemnified party, generally their business partners or customers, in connection with any U.S. patent, or any copyright or other intellectual property infringement claim by any third party with respect to our products. The term of these indemnification agreements is generally perpetual anytime after the execution of the agreement. The maximum potential amount of future payments we could be required to make under these agreements is unlimited. We have never incurred costs to defend lawsuits or settle claims related to these indemnification agreements. As a result, we believe the estimated fair value of these agreements is minimal.

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We have entered into indemnification agreements with our directors and officers that require us to (i) indemnify our directors and officers against liabilities that may arise by reason of their status or service as directors or officers, other than liabilities arising from willful misconduct of a culpable nature, (ii) advance their expenses incurred as a result of any proceeding against them as to which they could be indemnified; and (iii) obtain directors' and officers' insurance if available on reasonable terms, which we currently have in place.

Product Warranty

We provide warranties for our products for a specific period of time, generally twelve months, against material defects. We provide for the estimated future costs of warranty obligations in cost of sales when the related revenue is recognized. The accrued warranty costs represent the best estimate at the time of sale of the total costs that we expect to incur to repair or replace product parts that fail while still under warranty. The amount of accrued estimated warranty costs are primarily based on historical experience as to product failures as well as current information on repair costs. On a quarterly basis, we review the accrued balances and update these based on the historical warranty cost trends. The following table reflects the change in our warranty accrual which is included in "accrued liabilities" on the condensed consolidated balance sheets, during the three months ended March 31, 2014 and 2013 (in thousands):

	Three Months Ended March 31, 2014			2013		
Beginning accrued warranty and related costs	$	1048		$	588	
Accruals for warranties issued		496			264	
Adjustments related to pre-existing warranties including expirations and changes in estimates		(103	)		166	
Cost of warranty repair		(214	)		(269	)
Ending accrued warranty and related costs	$	1,227		$	749	

Contractual Obligations

We lease certain office space, manufacturing facilities and equipment under long-term operating leases expiring at various dates through February 2023. The majority of our lease obligations relates to our lease agreement for the facility at Fremont, California with approximately 27,760 square feet, which commenced on December 1, 2008 for a term of seven years, with an option by us to cancel the lease after five years, upon forfeiture of the security deposit and payment of one-half of the fifth year's rent. On June 28, 2013, we sent a notice to terminate the lease effective November 30, 2013 with an early termination penalty of $142,000 which was recorded as an expense in the third quarter of 2013. On August 2, 2013, we signed a new lease agreement for the current facility with reduced footage of 20,767 square feet, which commenced on December 1, 2013 for a term of two years. The reduced square footage, the reduced rate per square foot, and the expected reduced operating costs, would save us approximately total $382,000 during 2014 and 2015.

We entered into a royalty agreement with a vendor effective December 3, 2010 with a term of eight years, terminating December 31, 2018. We and our related companies are granted a worldwide, nonexclusive, royalty bearing, irrevocable license to certain patents for the term of the agreement. We shall pay a total of $7.0 million royalty payment over eight years beginning in 2011 based on future royalty bearing sales. This agreement contains a clause that allows us to make a claim for credit, starting in 2013, in the event that the royalty bearing sales for the year is lower than a pre-determined amount set forth in this agreement.

Outstanding contractual obligations as of March 31, 2014 are summarized as follows (in thousands):

	Payments due by period				
Contractual Obligations	Total	Less than 1 year	1-3 years	4-5 years	More than 5 years
Operating leases	$557	$263	$		