

ELXSI Corporation

Quarterly Consolidated Financial Statements (Unaudited)

June 30, 2016

ELXSI CORPORATION
CONSOLIDATED BALANCE SHEETS
(Amounts in Thousands, Except Share and Per Share Data)
(Unaudited)

ASSETS

	<u>June 30,</u> <u>2016</u>	<u>December 31,</u> <u>2015</u>
Current assets:		
Cash and cash equivalents	\$ 17,536	\$ 16,642
Accounts receivable, less allowance for doubtful accounts of \$329 and \$334 in 2016 and 2015, respectively	14,523	9,299
Inventories, net	21,152	22,257
Prepaid expenses and other current assets	<u>803</u>	<u>503</u>
Total current assets	54,014	48,701
Property, buildings and equipment, net	7,196	7,132
Deferred income taxes	14,402	16,790
Other	<u>49</u>	<u>84</u>
Total assets	<u>\$ 75,661</u>	<u>\$ 72,707</u>

(Continued)

ELXSI CORPORATION
CONSOLIDATED BALANCE SHEETS (Continued)
(Amounts in Thousands, Except Share and Per Share Data)
(Unaudited)

LIABILITIES AND STOCKHOLDERS' EQUITY

	June 30, <u>2016</u>	December 31, <u>2015</u>
Current liabilities:		
Accounts payable	\$ 3,609	\$ 3,393
Accrued expenses	6,920	5,742
Capital lease obligations - current	<u>47</u>	<u>48</u>
Total current liabilities	10,576	9,183
Capital lease obligations - noncurrent	123	147
Deferred financing obligations	555	587
Phantom stock payable	<u>--</u>	<u>2,854</u>
Total liabilities	<u>11,254</u>	<u>12,771</u>
Commitments and contingencies		
Stockholders' equity:		
Preferred Stock, par value \$0.002 per share		
Authorized--5,000,000 shares		
604,656 designated Series A Non-voting		
Convertible Preferred Stock		
Issued and outstanding--none	--	--
600,000 designated Series B Junior		
Participating Preferred Stock		
Issued and outstanding -- none	--	--
Common Stock, par value \$0.001 per share		
Authorized--60,000,000 shares		
Issued and outstanding—3,393,673 shares at		
June 30, 2016 and 3,406,957 shares at		
December 31, 2015	3	3
Additional paid-in-capital	208,989	209,235
Accumulated deficit	(144,248)	(148,652)
Accumulated other comprehensive loss	<u>(337)</u>	<u>(650)</u>
Total stockholders' equity	<u>64,407</u>	<u>59,936</u>
Total liabilities and stockholders' equity	<u>\$ 75,661</u>	<u>\$ 72,707</u>

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

ELXSI CORPORATION
CONSOLIDATED STATEMENTS OF INCOME AND COMPREHENSIVE INCOME
(Amounts in Thousands, Except Per Share Data)
(Unaudited)

	Three Months Ended		Six Months Ended	
	June 30,		June 30,	
	<u>2016</u>	<u>2015</u>	<u>2016</u>	<u>2015</u>
Net sales	\$ 24,666	\$ 22,318	\$ 47,919	\$ 41,331
Costs and expenses:				
Cost of sales	16,089	13,986	31,775	26,977
Selling, general and administrative	4,215	4,549	8,410	8,804
Depreciation	<u>268</u>	<u>309</u>	<u>542</u>	<u>625</u>
	<u>20,572</u>	<u>18,844</u>	<u>40,727</u>	<u>36,406</u>
Gain from restaurant closures and lease termination costs and sales of property and buildings	<u>--</u>	<u>10</u>	<u>254</u>	<u>10</u>
Operating income	4,094	3,484	7,446	4,935
Other income (expense):				
Interest expense	(51)	(81)	(128)	(159)
Interest income	50	6	50	10
Other income	<u>45</u>	<u>4</u>	<u>95</u>	<u>5</u>
Income before provision for income taxes	4,138	3,413	7,463	4,791
Provision for income taxes	<u>(1,697)</u>	<u>(332)</u>	<u>(3,059)</u>	<u>(431)</u>
Net income	2,441	3,081	4,404	4,360
Other comprehensive income (loss)				
Foreign currency translation adjustment, net of tax:	<u>43</u>	<u>29</u>	<u>313</u>	<u>(109)</u>
Comprehensive income	<u>\$ 2,484</u>	<u>\$ 3,110</u>	<u>\$ 4,717</u>	<u>\$ 4,251</u>
Earnings per common share:				
Basic	<u>\$ 0.72</u>	<u>\$ 0.91</u>	<u>\$ 1.30</u>	<u>\$ 1.29</u>
Diluted	<u>\$ 0.67</u>	<u>\$ 0.85</u>	<u>\$ 1.20</u>	<u>\$ 1.23</u>
Weighted average number of common and common equivalent shares				
Basic	<u>3,397</u>	<u>3,396</u>	<u>3,400</u>	<u>3,385</u>
Diluted	<u>3,667</u>	<u>3,537</u>	<u>3,670</u>	<u>3,543</u>

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

ELXSI CORPORATION
CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY
(Dollars in Thousands)
(Unaudited)

	<u>Common Stock</u>		<u>Additional</u>	<u>Accum-</u>	<u>Accumulated</u>	<u>Total</u>
	<u>Shares</u>	<u>Dollars</u>	<u>Paid-In-</u>	<u>ulated</u>	<u>Other</u>	
			<u>Capital</u>	<u>Deficit</u>	<u>Comprehensive</u>	
					<u>Loss</u>	
Balances at December 31, 2015	3,406,957	\$ 3	\$ 209,235	\$ (148,652)	\$ (650)	\$ 59,936
Other comprehensive income	--	--	--	--	313	313
Purchase and retirement of common stock	(13,284)	--	(246)	--	--	(246)
Net income	--	--	--	4,404	--	4,404
Balances at June 30, 2016	<u>3,393,673</u>	<u>\$ 3</u>	<u>\$ 208,989</u>	<u>\$ (144,248)</u>	<u>\$ (337)</u>	<u>\$ 64,407</u>

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

ELXSI CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Dollars in Thousands)
(Unaudited)

	Six Months Ended June 30,	
	2016	2015
Cash flows from operating activities:		
Net income	\$ 4,404	\$ 4,360
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	542	625
Amortization of other assets – software development costs	67	92
Amortization of deferred debt costs	13	13
Provision for obsolete and slow moving inventories	650	350
Gain on restaurant closures and lease termination costs and sales of property, buildings and equipment	(254)	(10)
Deferred income taxes	2,388	--
(Increase) decrease in assets:		
Accounts receivable	(5,224)	(1,386)
Inventories	544	(2,045)
Prepaid expenses and other current assets	(300)	(364)
Increase (decrease) in liabilities:		
Accounts payable	216	804
Accrued expenses	1,178	1,453
Net cash provided by operating activities	4,224	3,892
Cash flows from investing activities:		
Purchases of property, buildings and equipment	(888)	(598)
Other assets – software development costs	(48)	(58)
Proceeds from sale of property, buildings and equipment	450	14
Net cash used in investing activities	(486)	(642)
Cash flows from financing activities:		
Principal payment of phantom stock payable	(2,854)	--
Purchase and retirement of common stock	(246)	(326)
Principal payments on deferred financing obligations	(32)	(28)
Principal payments on capital lease obligations	(25)	(24)
Net cash used in financing activities	(3,157)	(378)
Effect of exchange rate changes on cash and cash equivalents:	313	(109)

(Continued)

ELXSI CORPORATION
CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)
(Dollars in Thousands)
(Unaudited)

	<u>Six Months Ended June 30,</u>	
	<u>2016</u>	<u>2015</u>
Increase in cash and cash equivalents	894	2,763
Cash and cash equivalents, beginning of period	<u>16,642</u>	<u>7,123</u>
Cash and cash equivalents, end of period	<u>\$ 17,536</u>	<u>\$ 9,886</u>

Supplemental Disclosure of Cash Flow Information:

Cash paid during the period for:		
Income taxes	\$ 243	\$ 366
Interest	\$ 53	\$ 147

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

ELXSI CORPORATION
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
June 30, 2016
(Unaudited)

Note 1. The Company

General. ELXSI Corporation (together with its subsidiaries, the “Company”) currently operates through its two wholly-owned subsidiaries, ELXSI, a California corporation (“ELXSI”), and Bickford’s Family Restaurants, Inc., a Delaware corporation (“BFRI”). Operations consist of the following business segments: an equipment manufacturer headquartered in Orlando, Florida and a restaurant chain in New England.

Equipment Manufacturer. Cues of Orlando, Florida operates as a division of ELXSI. Cues is engaged in the manufacturing and servicing of robotic video inspection, repair equipment and software for wastewater and drainage systems primarily for municipalities, service contractors and industrial users throughout the United States of America and internationally. Cues sells and services its products in Canada through ELXSI’s wholly-owned subsidiary Cues Canada, which is located in Ontario, Canada.

Restaurant Operations. As of June 30, 2016, the Company, through BFRI, has four operating restaurants (hereinafter referred to as the “Restaurants” or “Restaurant Operations”) located in Massachusetts. In addition to the four operating Restaurants, the Company leased four other restaurant properties that were no longer being operated by the Company and are subleased or assigned to third parties.

In March 2016, BFRI sold its rights associated with the lease and assets of the Salem, New Hampshire location and consequently ceased operations in that location. As a result of the transaction, the Company recorded the proceeds from the sale of this property in the amount of \$450,000 and recognized a gain on this sale of approximately \$254,000.

Note 2. Basis of Presentation

The unaudited consolidated financial statements included herein have been prepared by the Company, without audit or review, and in accordance with accounting principles generally accepted in the United States of America (“US GAAP”) for interim financial reporting. Certain information and note disclosures normally included in financial statements prepared in accordance with US GAAP have been omitted, although the Company believes that the disclosures are adequate to make the information presented not misleading. It is suggested that these financial statements be read in conjunction with the Company’s audited consolidated financial statements and the notes thereto as of and for the year ended December 31, 2015. In the opinion of the Company, all adjustments (solely of a normal recurring nature) necessary to present fairly the consolidated financial position of the Company and its subsidiaries as of June 30, 2016, and the results of their operations and cash flows for the three and six months ended June 30, 2016, have been included in these unaudited consolidated financial statements. Readers of these financial statements are cautioned, however, that the results of operations for such interim periods are not necessarily indicative of the results for the subsequent interim periods or the entire year.

Note 3. Earnings Per Share

The Company presents basic earnings per share, which is net income divided by weighted average shares outstanding during the period and diluted earnings per share, which considers the impact of common stock equivalents. The Company's common stock equivalents consist of a common stock grant. As of June 30, 2016, the Company had 270,000 common stock equivalents outstanding under the common stock grant. There were 95,000 common stock equivalents outstanding as of December 31, 2015.

Note 4. Fair Value of Financial Instruments

The carrying amount of the Company's financial instruments, including cash and cash equivalents, accounts receivable, accounts payable and accrued expenses approximates fair value due to the short-term maturity of those instruments.

Note 5. Composition of Inventories

Inventories are summarized in the following table.

	June 30, 2016 <u>(unaudited)</u>	December 31, 2015 <u></u>
Inventories:		
Raw materials and finished goods	\$ 17,529,000	\$ 16,971,000
Work in process	<u>8,703,000</u>	<u>9,727,000</u>
	26,232,000	26,698,000
Less: reserve for slow moving and obsolete inventories	<u>(5,080,000)</u>	<u>(4,441,000)</u>
	<u>\$ 21,152,000</u>	<u>\$ 22,257,000</u>

Note 6. Income Taxes

Income (loss) before provision for income taxes for the six months ended June 30, 2016 and 2015 were as follows:

	<u>2016</u>	<u>2015</u>
Domestic	\$ 7,745,000	\$ 4,978,000
Foreign	<u>(282,000)</u>	<u>(187,000)</u>
Total	<u>\$ 7,463,000</u>	<u>\$ 4,791,000</u>

The components of provision for income taxes for the six months ended June 30, 2016 and 2015 were as follows:

	<u>2016</u>	<u>2015</u>
Current - Federal, state and local	\$ 671,000	\$ 431,000
Deferred – Federal, state and local	<u>2,388,000</u>	<u>--</u>
Total	<u>\$ 3,059,000</u>	<u>\$ 431,000</u>

Note 7. Long-Term Debt

The Company chose not to renew its \$6,000,000 revolving credit facility (“Credit Facility”) with Wells Fargo Bank N.A. that expired on June 30, 2016. As of June 30, 2016 and December 31, 2015, no amounts were outstanding under the Credit Facility.

Note 8. Phantom Stock Option Plan. The ELXSI phantom stock option plan was implemented in 1992 as a long-term incentive plan for key executives of the Restaurants (the “Group”).

On July 2, 2001, the Group exercised in full their rights to receive payment under this plan. In March 2003, the Company reached agreements with the Group under which they were to receive principal payments totaling \$2,854,000. However, principal payments are subject to the approval of the Board of Directors of the Company. Unpaid principal bore interest at a fixed rate of 7% per annum.

As of December 31, 2015, a liability totaling \$2,854,000 was included in the accompanying consolidated balance sheets. During 2015, the Company recorded no compensation expense related to the phantom stock option plan and approximately \$200,000 in interest expense for the full year.

In May 2016, the Board of Directors authorized the full principal payment in the amount of \$2,854,000. In connection with the payment, the Company recorded approximately \$59,000 in expense during the six months ended June 30, 2016.

During the six months ended June 30, 2016 and 2015, the Company recorded interest expense related to the phantom stock option plan of approximately \$72,000 and \$99,000, respectively.

Note 9. Segment Reporting.

The Company has two reportable segments, equipment manufacturing (“Equipment”) and restaurant operations (“Restaurants”). See also Note 1. The Company is primarily organized into two strategic business units, which have separate management teams and infrastructures and that offer different products and services. Each business requires different employee skills, technology and marketing strategies. The equipment manufacturing segment produces sewer inspection equipment and software for sale to municipalities, contractors, and foreign governments. As of June 30, 2016 and 2015, the restaurant operations segment includes Restaurants located in Massachusetts operating under the Bickford’s brand name.

The Company evaluates the performance of each segment based upon profit or loss from operations before income taxes, non-recurring gains and losses and foreign exchange gains and losses.

Summarized financial information by business segment for the six months ended June 30, 2016 and 2015 is summarized in the following table. The other lines include corporate related items and results of insignificant operations.

	<u>2016</u>	<u>2015</u>
Net Sales to External Customers:		
Equipment	\$ 44,515,000	\$ 37,461,000
Restaurants	<u>3,404,000</u>	<u>3,870,000</u>
	<u>\$ 47,919,000</u>	<u>\$ 41,331,000</u>
Segment Assets:		
Equipment	\$ 45,674,000	\$ 39,226,000
Restaurants	1,609,000	1,830,000
Other	<u>28,378,000</u>	<u>9,269,000</u>
	<u>\$ 75,661,000</u>	<u>\$ 50,325,000</u>
Capital Expenditures for Segment Assets:		
Equipment	\$ 883,000	\$ 578,000
Restaurants	<u>5,000</u>	<u>20,000</u>
	<u>\$ 888,000</u>	<u>\$ 598,000</u>
Depreciation:		
Equipment	\$ 475,000	\$ 551,000
Restaurants	62,000	69,000
Other	<u>5,000</u>	<u>5,000</u>
	<u>\$ 542,000</u>	<u>\$ 625,000</u>
Interest Expense:		
Restaurants	\$ 35,000	\$ 39,000
Other	<u>93,000</u>	<u>120,000</u>
	<u>\$ 128,000</u>	<u>\$ 159,000</u>

Summarized financial information by business segment for the three months ended June 30, 2016 and 2015 is summarized in the following table.

	<u>2016</u>	<u>2015</u>
Net Sales to External Customers:		
Equipment	\$ 23,013,000	\$ 20,362,000
Restaurants	<u>1,653,000</u>	<u>1,956,000</u>
	<u>\$ 24,666,000</u>	<u>\$ 22,318,000</u>
Depreciation:		
Equipment	\$ 237,000	\$ 272,000
Restaurants	28,000	34,000
Other	<u>3,000</u>	<u>3,000</u>
	<u>\$ 268,000</u>	<u>\$ 309,000</u>
Interest Expense:		
Restaurants	\$ 17,000	\$ 20,000
Other	<u>34,000</u>	<u>61,000</u>
	<u>\$ 51,000</u>	<u>\$ 81,000</u>

There were no inter-segment sales or transfers during the three and six months ended June 30, 2016 and 2015. Foreign assets represented less than 10% of the Company's totals. During the six months ended June 30, 2016 and 2015 foreign sales represented 5.2% and 3.6%, respectively of total sales. No material amounts of the Company's sales depended upon a single customer.