

HUGHES Telematics, Inc.
Form 10-Q
May 10, 2011
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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

x Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 for the quarterly period ended March 31, 2011, or

o Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934
Commission file number 001-33860
HUGHES Telematics, Inc.
(Exact name of registrant as specified in its charter)

Delaware 26-0443717
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification Number)

2002 Summit Boulevard, Suite 1800 30319
Atlanta, Georgia
(Address of principal executive offices) (Zip Code)

Registrant's telephone number, including area code: (404) 573-5800

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes o 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 definition of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

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

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

As of May 9, 2011, 94,103,976 shares of the registrant's common stock were outstanding.

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PART I – FINANCIAL INFORMATION

Item 1. Financial Statements

HUGHES TELEMATICS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(Unaudited)

(In thousands, except share data)

	March 31, 2011	December 31, 2010
Assets		
Current assets:		
Cash and cash equivalents	\$25,003	\$14,596
Short-term investments	1,111	2,263
Accounts receivable, net	5,042	10,661
Prepaid expenses	808	933
Other current assets	2,868	3,078
Total current assets	34,832	31,531
Restricted cash	1,291	1,333
Property and equipment, net	23,276	24,516
Capitalized software, net	19,141	18,476
Intangible assets, net	11,738	12,591
Goodwill	5,169	5,169
Debt issuance costs	3,669	3,958
Other assets	11,002	11,243
Total assets	\$110,118	\$108,817
Liabilities and Stockholders' Deficit		
Current liabilities:		
Accounts payable	\$6,187	\$6,688
Accrued liabilities	21,888	18,868
Deferred revenue	16,282	12,972
Current portion of capital lease obligations	1,717	1,772
Current portion of long-term debt	5,527	5,632
Other current liabilities	1,108	1,585
Total current liabilities	52,709	47,517
Long-term debt, net of current portion	108,792	102,669
Capital lease obligations	136	152
Long-term deferred revenue	23,770	19,337
Other liabilities	1,557	1,504
Total liabilities	186,964	171,179
Commitments and contingencies (Note 11)		
Stockholders' deficit:		
Preferred stock, \$0.0001 par value. Authorized 10,000,000 shares, no shares issued and outstanding at March 31, 2011 and December 31, 2010	—	—
Common stock, \$0.0001 par value. Authorized 155,000,000 shares; issued and outstanding 94,103,976 shares at March 31, 2011 and 92,675,404 shares at December 31, 2010	9	9
Additional paid-in capital	377,149	370,229
Accumulated deficit	(467,276)	(445,450)
Total HUGHES Telematics, Inc. stockholders' deficit	(90,118)	(75,212)
Non-controlling interests in consolidated subsidiary	13,272	12,850
Total stockholders' deficit	(76,846)	(62,362)

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Total liabilities and stockholders' deficit	\$110,118	\$108,817
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The accompanying notes are an integral part of these condensed consolidated financial statements.

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HUGHES TELEMATICS, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
 (Unaudited)
 (In thousands, except share data)

	Three Months Ended March	
	31,	
	2011	2010
Revenues:		
Services	\$13,601	\$6,056
Hardware	2,362	2,111
Total revenues	15,963	8,167
Operating costs and expenses (exclusive of depreciation and amortization shown separately):		
Cost of services	5,867	5,228
Cost of hardware sold	1,567	1,587
Research and development	4,278	2,020
Sales and marketing	6,904	5,132
General and administrative	10,834	8,185
Depreciation and amortization	3,528	3,481
Total operating costs and expenses	32,978	25,633
Loss from operations	(17,015)	(17,466)
Interest income	12	48
Interest expense	(5,716)	(5,296)
Loss before income taxes	(22,719)	(22,714)
Income tax expense	—	—
Net loss	(22,719)	(22,714)
Net loss attributable to non-controlling interests	893	—
Net loss attributable to HUGHES Telematics, Inc.	\$(21,826)	\$(22,714)
Basic and diluted loss per common share	\$(0.64)	\$(0.85)
Basic and diluted weighted average common shares outstanding	34,178,501	26,572,440
The accompanying notes are an integral part of these condensed consolidated financial statements.		

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HUGHES TELEMATICS, INC.
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
 (Unaudited)
 (In thousands)

	Three Months Ended March 31,	
	2011	2010
Cash flows from operating activities:		
Net loss	\$(22,719)	\$(22,714)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	3,528	3,481
Interest expense on long-term debt and capital leases	1,246	3,794
Amortization of debt issuance costs and discounts on long-term debt	1,750	1,502
Share-based compensation expense	840	587
Non-cash services contributed to consolidated subsidiary by non-controlling interests	544	—
Loss (Gain) on disposal of assets	8	(7)
Changes in assets and liabilities:		
Accounts receivable, net	5,619	1,370
Prepaid expenses and other assets	467	1,482
Accounts payable and accrued and other liabilities	2,098	(84)
Deferred revenue	7,742	582
Net cash provided by (used in) operating activities	1,123	(10,007)
Cash flows from investing activities:		
Purchases of short-term investments	(1,111)	(3,357)
Maturities of short-term investments	2,263	—
Purchases of property and equipment	(434)	(209)
Increase in capitalized software	(876)	(974)
Proceeds from disposal of assets	105	464
Decrease (Increase) in restricted cash	42	(206)
Net cash used in investing activities	(11)	(4,282)
Cash flows from financing activities:		
Proceeds from the issuance of common stock, net of costs	4,669	—
Proceeds from the issuance of long-term debt	5,000	—
Payment of debt issuance costs	(147)	—
Repayment of capital lease obligations	(122)	(1,416)
Repayment of long-term debt	(105)	(34)
Net cash provided by (used in) financing activities	9,295	(1,450)
Net increase (decrease) in cash and cash equivalents	10,407	(15,739)
Cash and cash equivalents, beginning of period	14,596	28,368
Cash and cash equivalents, end of period	\$25,003	\$12,629
Supplemental non-cash disclosure:		
Intangible assets and capitalized software costs contributed to consolidated subsidiary by non-controlling interests	\$739	\$—
Property and equipment acquired by capital lease obligations	\$—	\$277

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

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HUGHES TELEMATICS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

(1) Description of Business

HUGHES Telematics, Inc. (together with our consolidated subsidiaries, “we,” “us” and “our”) is a telematics services company that provides a suite of real-time voice and data communications services and applications for use in vehicles and is developing additional applications for use within and outside of the automotive industry. These services and applications are enabled through a state-of-the-art communications center designed with flexibility to connect various mobile devices with content, services and call centers. Within the automotive industry, our communications center allows for two way voice and data communications to vehicles and supports, among other things, critical safety and security services as well as location-based services and remote diagnostics. Since November 16, 2009, we have been the exclusive telematics service provider in the United States for all new vehicles sold by Mercedes-Benz USA, LLC (“Mercedes-Benz”), and we are now the preferred provider of telematics services for all Mercedes-Benz vehicles purchased prior to November 16, 2009. These services are marketed under the mbrace® brand. In addition, our In-Drive® solution offers services to consumers or other third parties through an aftermarket hardware device that we have developed and which we intend to distribute through relationships with companies and organizations with large customer or membership bases for installation in existing vehicles. We expect to launch our In-Drive solution in the third quarter of 2011 through an agreement with a large insurance company. Additionally, through Networkfleet, Inc. (“Networkfleet”), our wholly-owned subsidiary, we currently offer remote vehicle monitoring and other data services through after-market hardware that is purchased separately and installed in fleets of vehicles.

In May 2010, we broadened our connected services beyond the automotive market to include the mobile health and wellness industry with the formation of Lifecomm, LLC (“Lifecomm”), a majority owned subsidiary founded with QUALCOMM Incorporated (“Qualcomm”), a leader in developing and delivering innovative digital wireless communications products and services, and American Medical Alert Corp. (“AMAC”), a healthcare communications company dedicated to the provision of support services to the healthcare community. Lifecomm intends to design, develop, finance and operate a mobile personal emergency response service which will permit subscribers to initiate requests for emergency assistance services through a wearable device that is able to communicate information to and support voice interactions between the subscriber and an emergency assistance call center. Lifecomm expects to launch its service offerings in the fourth quarter of 2011.

(2) Basis of Presentation

We have prepared the accompanying condensed consolidated financial statements in accordance with United States generally accepted accounting principles (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Rule 10-01 of Regulation S-X and include our accounts and the accounts of our wholly-owned subsidiary, Networkfleet, and our majority-owned subsidiary, Lifecomm, for periods following the formation of Lifecomm. The accompanying condensed consolidated financial statements do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, the accompanying condensed consolidated financial statements contain all adjustments, consisting only of those of a normal recurring nature, necessary for a fair presentation of our financial position, results of operations and cash flows at the dates and for the periods indicated. While we believe that the disclosures presented are adequate to make the information not misleading, these condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements for the year ended December 31, 2010 and the related notes thereto which have been included in our annual report on Form 10-K filed with the Securities and Exchange Commission (the “SEC”) on March 16, 2011. The results of the three months ended March 31, 2011 are not necessarily indicative of the results to be expected for the full year. All intercompany balances and transactions have been eliminated. Certain prior period amounts have been reclassified to conform to current presentation.

During the three months ended March 31, 2011 and the years ended December 31, 2010, 2009 and 2008, we incurred a net loss of approximately \$22.7 million, \$89.6 million, \$163.7 million and \$57.5 million, respectively. Cash flow provided by operations was approximately \$1.1 million in the three months ended March 31, 2011, but we used cash

in operations of approximately \$25.1 million, \$47.2 million and \$39.1 million in the years ended December 31, 2010, 2009 and 2008, respectively. As of March 31, 2011, we had unrestricted cash, cash equivalents and short-term investments of approximately \$26.1 million and an accumulated deficit of approximately \$467.3 million. Of the cash, cash equivalents and short-term investments, approximately \$7.8 million is held by our Lifecomm subsidiary for use in that business. We believe that the cash and cash equivalents on hand and the projected cash flows to be generated by our service offerings to Mercedes-Benz vehicles and sales of our In-Drive and Lifecomm products and services will allow us to continue operations beyond the next twelve months. Since we launched our service offerings to Mercedes-Benz vehicles about a year and a half ago and expect to launch our In-Drive and Lifecomm products and services during the year ending December 31, 2011, some or all of the assumptions underlying our projections may prove to be materially inaccurate. If so, we cannot assure you that our net losses and negative cash flow will not surpass our expectations, and thus, we may be required to raise additional capital in the future or to reduce

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our operating expenditures. This additional financing may take the form of loans under a new credit facility, the issuance of bonds or other types of debt securities, the issuance of equity securities or a combination of the foregoing. Any such financing must either comply with the covenants of our existing credit facilities, or we will need to obtain waivers from the lenders. Our credit facilities contain covenants that restrict our ability to incur debt and will require mandatory prepayments from the proceeds of an equity financing. Any debt financing obtained may impose various restrictions and additional covenants on us which could limit our ability to respond to market conditions, provide for unanticipated capital investments or take advantage of business opportunities and may subject us to significant interest expense. Additional equity financing may be obtained on terms that are dilutive to the interests of existing stockholders. We have been successful in the past raising capital to address our liquidity needs; however, debt or additional equity financing may not be available when needed in the future on terms favorable to us or at all, and the failure to attract a sufficient amount of additional debt or equity capital may impair our ability to execute on our business plan. Such additional capital may be provided by, among other things, the cash proceeds from the exercise of the outstanding warrants to purchase shares of our common stock. There is no assurance that we will be successful in obtaining additional financing, if needed, or that we will be able to reduce our operating expenditures. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

(3)Lifecomm, LLC

In accordance with the applicable accounting guidance governing consolidation, we have determined that Lifecomm is a variable interest entity ("VIE") for which we are the primary beneficiary. Accordingly, we have included Lifecomm's financial position, results of operations and cash flows in our consolidated financial statements as of and for the three months ended March 31, 2011. As of March 31, 2011, Lifecomm's assets consisted of approximately \$6.7 million of cash and cash equivalents, approximately \$1.1 million of short-term investments that are held-to-maturity, \$3.0 million of intangible assets and approximately \$2.0 million of capitalized software costs, and its liabilities consisted of approximately \$1.5 million of accounts payable and accrued liabilities. As of December 31, 2010, Lifecomm's assets consisted of approximately \$7.8 million of cash and cash equivalents, approximately \$1.5 million of short-term investments that are held-to-maturity, \$3.0 million of intangible assets and approximately \$0.5 million of capitalized software costs, and its liabilities consisted of approximately \$1.2 million of accounts payable and accrued liabilities. Each of the initial members of Lifecomm have preemptive rights with respect to future issuances of securities by Lifecomm, as well as rights of first offer, drag-along and tag-along rights on transfers of securities by the other members. In addition, for a two year period beginning on May 12, 2014, any member (or group of members) holding at least 25% of the membership interests in Lifecomm will have the right to demand either an auction for the sale of Lifecomm or an initial public offering of Lifecomm. Should Lifecomm fail to achieve either of these liquidity events within 180 days of the demand, then to the extent at such time we hold at least 50% of the outstanding membership interests of Lifecomm and our common stock is publicly traded, each other member will be entitled on a one-time basis to exchange all of its membership interests in Lifecomm for shares of our common stock with equivalent fair market value. While we determined that such right to exchange is a freestanding derivative instrument, as the fair market value of our common stock to be issued in the exchange will be equal to the fair market value of the membership interests of Lifecomm received, the value of the derivative instrument is not material as of March 31, 2011.

(4)Recently Adopted Accounting Pronouncements

In September 2009, the EITF issued revised guidance governing certain revenue arrangements that include software elements, which amends the scope of existing guidance to exclude tangible products that include software and non-software components that function together to deliver the product's essential functionality. Additionally, the EITF issued revised guidance governing revenue arrangements with multiple deliverables, which provides a greater ability to separate and allocate the arrangement consideration in a multiple element revenue arrangement. The revised guidance requires the use of an estimated selling price to allocate arrangement consideration if vendor-specific objective evidence of selling price ("VSOE") is not available, and eliminates the residual method of allocation. This guidance was effective for us on January 1, 2011. We price and sell hardware and services separately based on VSOE, and account for hardware and services as separate units of accounting. The new accounting guidance did not have a material effect on our results of operations as it did not change our units of accounting or general timing of delivery or

performance.

(5) Long-Term Debt

The components of long-term debt were as follows:

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	March 31, 2011	December 31, 2010
	(in thousands)	
Senior secured term indebtedness	\$70,948	\$ 70,254
Second lien secured term indebtedness	16,674	12,250
Senior unsecured promissory note	5,527	5,632
Senior subordinated unsecured promissory notes	21,170	20,165
Total indebtedness	114,319	108,301
Less current portion	(5,527)	(5,632)
Total long-term debt, net of current portion	\$108,792	\$ 102,669
Senior Secured Term Indebtedness		

On March 31, 2008, we entered into a credit agreement (as amended and restated, the “First Lien Credit Agreement”) pursuant to which we issued in multiple tranches during the year ended December 31, 2008 for aggregate consideration of \$60.0 million, senior secured term indebtedness due March 31, 2013 with an original principal amount of \$60.0 million and warrants to purchase the equivalent of 4,801,112 shares of our common stock, comprised of 1,103,922 initial shares and 3,697,190 earn-out shares, at an equivalent exercise price of less than \$0.01 per share. The senior secured term indebtedness is guaranteed by all of our existing and future domestic subsidiaries and is secured by all of our tangible and intangible assets. At our election, the term indebtedness bears interest at (i) the Prime Lending Rate plus 10.00% or (ii) for Eurocurrency borrowings, 11.00% plus the greater of London Interbank Offered Rate (“LIBOR”) or 3.00%. In accordance with an agreement between us and one of the senior secured note holders, the interest rate on term indebtedness with an initial principal amount of \$5.0 million will have an interest rate of no higher than 14.00% for the term of the debt. With respect to Eurocurrency borrowings, we may elect interest periods of one, two, three, or six months (or nine or twelve months if approved by each senior secured note holder), and interest is payable in arrears at the end of each interest period but, in any event, at least every three months. With respect to all interest periods ending on or prior to March 31, 2010, the interest accrued on the senior secured term indebtedness was paid in kind in arrears with such accrued interest being added to the outstanding principal balance of the term indebtedness. With respect to all interest periods ending after March 31, 2010, the accrued interest will be paid in cash in arrears. As of each of March 31, 2011 and December 31, 2010, senior secured term indebtedness with an aggregate principal amount, including the accrued interest which had been paid in kind, of approximately \$76.9 million was outstanding. As of March 31, 2011, we had elected that all outstanding amounts consist of Prime Lending borrowings which resulted in the term indebtedness bearing an interest rate of 13.25%.

The First Lien Credit Agreement requires us to comply with negative covenants which include, among others, limitations on our ability to incur additional debt; create liens; pay dividends or make other distributions; make loans and investments; sell assets; redeem or repurchase capital stock or subordinated debt; engage in specified transactions with affiliates; consolidate or merge with or into, or sell substantially all of our assets to, another person; and enter into new lines of business. We may incur indebtedness beyond the specific limits allowed under the First Lien Credit Agreement, provided we maintain a leverage ratio of 5.0 to 1.0. In addition, we may incur limited indebtedness secured by junior and subordinated liens to the liens created under the First Lien Credit Agreement. Noncompliance with any of the covenants without cure or waiver would constitute an event of default. An event of default resulting from a breach of a covenant may result, at the option of the note holders, in an acceleration of the principal and interest outstanding. The First Lien Credit Agreement also contains other events of default (subject to specified grace periods), including defaults based on the termination of the Mercedes-Benz contract, events of bankruptcy or insolvency and nonpayment of principal, interest or fees when due. The First Lien Credit Agreement also requires us to use 25% of the net cash proceeds from certain equity issuances for the repayment of senior secured term indebtedness.

As of each issuance date, we ascribed value to the senior secured term indebtedness and the related warrants based on their relative fair values. As such, an aggregate of \$46.9 million was allocated to the senior secured term indebtedness and an aggregate of \$12.1 million was allocated to the warrants. The resulting discount from the face value of the senior secured term indebtedness resulting from the ascribed value to the warrants is being amortized as additional

interest expense over the term of the senior secured term indebtedness using the effective interest rate method. As of March 31, 2011, the fair value of the senior secured indebtedness approximated carrying value.

Second Lien Term Indebtedness

On December 17, 2009, we entered into a credit agreement (the "Second Lien Credit Agreement") with PLASE HT, LLC ("PLASE HT"), as administrative agent, collateral agent and original lender, pursuant to which we issued indebtedness due October 1, 2013 with an original principal amount of \$15.0 million and warrants to purchase 3,000,000 shares of common stock at an exercise price of \$6.00 per share. PLASE HT is an affiliate of Apollo Global Management LLC ("Apollo") and of

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our controlling stockholder, Communications Investors, LLC (“Communications LLC”). On February 7, 2011, we entered into an incremental loan commitment agreement with certain unaffiliated investors, pursuant to which we issued additional indebtedness under the Second Lien Credit Agreement with an original principal amount of \$5.0 million and warrants to purchase 1,000,000 shares of common stock at an exercise price of \$5.99 per share. The loans under the Second Lien Credit Agreement bear interest at 9.00% per annum, payable-in-kind, and are guaranteed by all of our existing and future domestic subsidiaries. The loans are secured by a second priority lien on substantially all of our tangible and intangible assets, including the equity interests of our subsidiaries. The liens granted in connection with the Second Lien Credit Agreement are expressly subject and subordinated to the liens securing our obligations under the First Lien Credit Agreement.

The covenants contained in the Second Lien Credit Agreement are substantially the same as those in the First Lien Credit Agreement. The Second Lien Credit Agreement requires us to comply with negative covenants which include, among others, limitations on our ability to incur additional debt; create liens; pay dividends or make other distributions; make loans and investments; sell assets; redeem or repurchase capital stock or subordinated debt; engage in specified transactions with affiliates; consolidate or merge with or into, or sell substantially all of our assets to, another person; and enter into new lines of business. We may incur indebtedness beyond the specific limits allowed under the Second Lien Credit Agreement, provided we maintain a leverage ratio of less than 5.0 to 1.0. The events of default under the Second Lien Credit Agreement include, among others, payment defaults; defaults under, or acceleration of, certain indebtedness; termination of our contract with Mercedes-Benz; breaches of covenants or representations and warranties; certain ERISA events; certain judgments; and bankruptcy and insolvency events. The occurrence of an event of default could result in the acceleration of the obligations under the Second Lien Credit Agreement.

We ascribed value to the indebtedness issued in connection with the Second Lien Credit Agreement and the related warrants based on their relative fair values. As such, for the loans issued on February 7, 2011 and December 17, 2009, we allocated approximately \$3.6 million and \$9.5 million, respectively, of the proceeds to the indebtedness and the remaining approximately \$1.4 million and \$5.5 million, respectively, to the warrants. The resulting discount from the face value of the indebtedness resulting from the ascribed value to the warrants will be amortized as additional interest expense over the term of the indebtedness using the effective interest rate method. As of March 31, 2011, the fair value of the indebtedness approximated carrying value.

Senior Unsecured Promissory Note

On December 18, 2009, we issued to Hughes Network Systems, LLC (“HNS”), a wholly-owned subsidiary of HUGHES Communications, Inc. (“HCI”), a senior unsecured promissory note with a principal amount of approximately \$8.3 million through the conversion of a trade accounts payable balance of approximately \$6.0 million and the approximately \$2.3 million outstanding balance on an equipment financing arrangement owed to HNS. The promissory note accrues interest at a rate of 12.00% per annum, compounded annually, and was to become due and payable on December 31, 2010. Pursuant to the terms of the promissory note, we were required to make scheduled principal payments of approximately \$0.8 million on April 15, 2010 and \$1.5 million on each of July 15, 2010 and October 15, 2010. In addition, subject to all restrictions in the First Lien Credit Agreement and the Second Lien Credit Agreement and certain other limitations, to the extent we sell any capital equipment purchased by us (or purchased by HNS on our behalf) for use in connection with the Telematics Agreement between the parties, but no longer needed by us, we are required to make payments on the promissory note equal to the proceeds from the sale of such capital equipment (net of any selling costs).

On November 5, 2010, we and HNS agreed to amend the promissory note to (i) extend the maturity date to December 31, 2011, (ii) revise the schedule of principal payments and (iii) provide that the approximately \$1.0 million of accrued and unpaid interest shall be paid on December 31, 2010 with all future accrued interest on the promissory note paid quarterly in arrears. Pursuant to the terms of the amended promissory note, we made scheduled principal payments of \$0.5 million on each of October 15, 2010, December 31, 2010 and April 15, 2011 and are required to make scheduled principal payments of approximately \$0.8 million on July 15, 2011, \$1.5 million on October 15, 2011 and the balance on December 31, 2011. In connection with the amendment to the promissory note, we issued 50,000 shares of common stock to HNS as an amendment fee.

Senior Subordinated Unsecured Promissory Notes

On March 31, 2008, we issued to Communications LLC a senior subordinated unsecured promissory note with a principal amount of \$12.5 million and a maturity date of October 1, 2013. The note bears interest at a rate of 15.00% per annum which is compounded and added to the principal amount annually and is payable at maturity. In connection with the issuance of the note, we recorded a deemed capital contribution of approximately \$2.4 million related to the difference between (i) the fair value of the note using an estimated interest rate we would have paid an unrelated third party on a similar note and (ii) the fair value of the note using the 15.00% stated interest rate. The discount from the face value of the note resulting from the deemed capital contribution will be amortized as additional interest expense over the term of the note using the effective interest rate method.

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On December 12, 2008, we issued to Apollo Investment Fund V (PLASE) LP (“AIF V PLASE”) an additional senior subordinated unsecured promissory note with a principal amount of \$3.5 million and a maturity date of October 1, 2013. The note bears interest at 15.00% per annum which is compounded and added to the principal amount annually and is payable at maturity. In connection with the issuance of the note, we recorded an additional deemed capital contribution of approximately \$2.4 million related to the difference between (i) the fair value of the note using an estimated interest rate we would have paid an unrelated third party on a similar note and (ii) the fair value of the note using the 15.00% stated interest rate. The discount from the face value of the note resulting from the deemed capital contribution will be amortized as additional interest expense over the term of the note using the effective interest rate method.

At the time of issuance of each promissory note, we determined the estimated fair value amount by using available market information and commonly accepted valuation methodologies. However, considerable judgment is required in interpreting market data to develop estimates of fair value. Accordingly, the fair value estimates presented herein are not necessarily indicative of the amounts that we or holders of the instruments could realize in a current market exchange. The use of different assumptions and/or estimation methodologies may have a material effect on the estimated fair value. As of March 31, 2011, the fair value of the senior subordinated unsecured promissory notes approximated carrying value.

(6) Stockholders’ Equity

On February 7, 2011, we completed a private placement of 1,428,572 shares of common stock to a group of accredited investors at a purchase price of \$3.50 per share. The aggregate purchase price for the common stock sold in the private placement was approximately \$5.0 million. In connection with the private placement, we entered into an amendment to the First Lien Credit Agreement providing for the waiver of the requirement to use 25% of the net cash proceeds from the private placement for the repayment of senior secured term indebtedness.

(7) Share-Based Compensation

In accordance with the applicable accounting guidance governing share-based payments, we record compensation expense for all share-based awards issued. For the three months ended March 31, 2011 and 2010, we recorded approximately \$0.8 million and \$0.6 million of compensation expense, respectively, related to share-based grants. Such compensation expense is included in research and development, sales and marketing and general and administrative expense in the accompanying consolidated statements of operations.

Stock Options

The following table reflects stock option activity for the three months ended March 31, 2011:

	Number of Shares	Weighted Average Exercise Price	Aggregate Intrinsic Value (in thousands)
Outstanding at December 31, 2010	3,800,957	\$3.33	
Granted	—	\$—	
Forfeited	—	\$—	
Outstanding at March 31, 2011	3,800,957	\$3.33	\$4,074
Exercisable at March 31, 2011	427,230	\$2.75	\$609

The following table provides information about stock options that are outstanding and exercisable as of March 31, 2011:

Exercise Price	Stock Options Outstanding			Stock Options Exercisable		
	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Life (Yrs)	Number of Shares	Weighted Average Exercise Price	Weighted Average Remaining Life (Yrs)

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\$1.65 - \$2.05	719,241	\$1.76	7.0	88,996	\$1.65	6.1
\$2.47	1,453,230	\$2.47	6.7	246,361	\$2.47	6.7
\$3.15 - \$3.40	356,000	\$3.33	8.9	30,000	\$3.23	8.7
\$5.19	1,272,486	\$5.19	8.2	61,873	\$5.19	8.2

For stock option awards outstanding as of March 31, 2011, we expect to recognize approximately \$3.4 million of additional compensation expense over the remaining average service period of approximately 1.2 years.

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Restricted Stock

The following table reflects restricted stock activity:

	Number of Shares	Weighted Average Grant Date Fair Value
Outstanding at December 31, 2010	839,280	\$4.05
Vested	(96,000)	\$4.01
Outstanding at March 31, 2011	743,280	\$4.06

For restricted stock awards outstanding as of March 31, 2011, we expect to record approximately \$1.6 million of additional compensation expense over the remaining average service period of approximately 0.7 years.

(8) Loss Per Common Share

Basic loss per common share is computed by dividing net loss attributable to common stockholders by the weighted average number of common shares outstanding for the period. Diluted loss per common share reflects the potential dilution from the exercise or conversion of securities into common stock. The potential dilutive effect of outstanding stock options and warrants is calculated using the "treasury stock" method.

During all periods presented, we had potential common shares that could dilute basic loss per common share in the future but have been excluded from the computation of diluted loss per common share as the effect would have been anti-dilutive. For the three months ended March 31, 2011 and 2010, there were 82,785,548 and 83,623,560 potential common shares, respectively, excluded from the computation of diluted loss per share, consisting primarily of shares of common stock issuable upon the exercise of outstanding stock options and warrants and shares of common stock held in escrow to be released to certain stockholders upon achievement of the specified price targets.

(9) Comprehensive Loss

Comprehensive loss is defined as the change in equity during a period from transactions and other events and circumstances from nonowner sources. Our comprehensive loss for each of the three months ended March 31, 2011 and 2010 equaled our net loss.

(10) Related Party Transactions

Apollo Global Management, LLC

Communications LLC, AIF V PLASE and PLASE HT are each affiliated with Apollo. As of March 31, 2011, Apollo, through these entities, owned approximately 61% of our outstanding common stock. HCI, also an affiliate of Apollo, owned an additional approximately 4% of our outstanding common stock. In December 2009, AIF V PLASE transferred its ownership in all of its equity and debt interests of us, including its holding of senior secured term indebtedness, the senior subordinated unsecured promissory note and common stock, to PLASE HT.

As of March 31, 2011, the affiliates of Apollo, not including HNS which is discussed below, collectively held an aggregate face value and accrued interest of \$5.9 million of senior secured term indebtedness, \$16.8 million of second lien secured term indebtedness and \$23.6 million of senior subordinated unsecured promissory notes.

Hughes Network Systems, LLC

For the three months ended March 31, 2011 and 2010, HNS, a wholly-owned subsidiary of HCI and an affiliate of Apollo, provided no and approximately \$0.3 million of services, respectively, to us. As of March 31, 2011 and December 31, 2010, we had no outstanding balance, not including the promissory note discussed below, payable to HNS.

On December 18, 2009, we issued to HNS a senior unsecured promissory note with a principal amount of approximately \$8.3 million through the conversion of a trade accounts payable balance of approximately \$6.0 million and the approximately \$2.3 million outstanding balance on an equipment financing arrangement owed to HNS. The promissory note accrues interest at a rate of 12.00% per annum, compounded annually, and was to become due and payable on December 31, 2010. Pursuant to the terms of the promissory note, we were required to make scheduled principal payments of approximately \$0.8 million on April 15, 2010 and \$1.5 million on each of July 15, 2010 and October 15, 2010. In addition, subject to all restrictions in the First Lien Credit Agreement and the Second Lien Credit

Agreement and certain other limitations, to the extent we sell any capital equipment purchased by us (or purchased by HNS on our behalf) for use in connection with the Telematics Agreement

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between the parties, but no longer needed by us, we are required to make payments on the promissory note equal to the proceeds from the sale of such capital equipment (net of any selling costs).

On November 5, 2010, we and HNS agreed to amend the promissory note to (i) extend the maturity date to December 31, 2011, (ii) revise the schedule of principal payments and (iii) provide that the approximately \$1.0 million of accrued and unpaid interest shall be paid on December 31, 2010 with all future accrued interest on the promissory note paid quarterly in arrears. Pursuant to the terms of the amended promissory note, we made scheduled principal payments of \$0.5 million on each of October 15, 2010, December 31, 2010 and April 15, 2011 and are required to make scheduled principal payments of approximately \$0.8 million on July 15, 2011, \$1.5 million on October 15, 2011 and the balance on December 31, 2011. In connection with the amendment to the promissory note, we issued 50,000 shares of common stock to HNS as an amendment fee.

Trivergance Business Resources, LLC

For each of the three months ended March 31, 2011 and 2010, Trivergance Business Resources, LLC, an affiliate of a member of our board of directors, provided approximately \$0.4 million of services to us.

(11) Commitments and Contingencies

Contractual Payment Obligations

We have a long-term contract with an automaker pursuant to which the automaker agreed to install telematics devices in its vehicles and permit us to exclusively provide telematics services to its new customers. This contract also required us to pay the automaker for certain non-recurring costs associated with the initiation of telematics services. Pursuant to the contract, we are currently committed to pay the automaker \$4.0 million during the year ending December 31, 2011.

Litigation and Claims

From time to time, we are subject to litigation in the normal course of business. We are of the opinion that, based on information presently available, the resolution of any such legal matters will not have a material adverse effect on our financial position, results of operations or our cash flows.

(12) Segment Information

We present our segment information along the same lines that our chief executive officer reviews our operating results in assessing performance and allocating resources. Accordingly, our operations have been classified into three business segments: (i) the HUGHES Telematics segment, which provides and is further developing the telematics solution which is being marketed to automakers and other parties and includes the operations relating to the contract with Mercedes-Benz and our In-Drive product offering; (ii) the Networkfleet segment, which provides an aftermarket wireless fleet management solution targeted to the local fleet market, and (iii) the Lifecomm segment, which is developing and will operate a mobile personal emergency response service which will permit subscribers to initiate requests for emergency assistance services through a wearable device.

The following table presents certain financial information on our reportable segments:

	Three Months Ended March 31,	
	2011	2010
	(in thousands)	
Revenues:		
HUGHES Telematics	\$ 6,541	\$ 21
Networkfleet	9,422	8,146
Lifecomm	—	—
Total	\$ 15,963	\$ 8,167
(Loss) Income from operations:		
HUGHES Telematics	\$ (14,518)	\$ (17,777)
Networkfleet	(446)	311
Lifecomm	(2,051)	—
Total	\$ (17,015)	\$ (17,466)

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	March 31, 2011	December 31, 2010
	(in thousands)	
Total assets:		
HUGHES Telematics	\$80,107	\$ 77,711
Networkfleet	17,143	18,235
Lifecomm	12,871	12,871
Total	\$110,121	\$ 108,817

Substantially all of our assets are located within the United States. As of March 31, 2011 and December 31, 2010, we included the approximately \$5.2 million of goodwill in the total assets of the Networkfleet segment.

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

The following discussion and analysis of our financial condition and results of operations are based upon financial statements which have been prepared in accordance with GAAP and should each be read together with our consolidated financial statements and the notes to those consolidated financial statements included elsewhere in this report. This report contains forward-looking statements that involve risks and uncertainties, including statements regarding our capital needs, business strategy, expectations and intentions within the meaning of Private Securities Litigation Reform Act of 1995 which represent our expectations or beliefs concerning future events. We urge you to consider statements that use the terms "believe," "do not believe," "anticipate," "expect," "plan," "may," "estimate," "strive," "will," "should," and variations of these words or similar expressions are intended to identify forward-looking statements. These statements reflect our current views with respect to future events and because our business is subject to numerous risks, and uncertainties, our actual results could differ materially from those anticipated in the forward-looking statements, including those set forth below under this "Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations" and elsewhere in this report. All forward-looking statements speak only as of the date of this report. Actual results will most likely differ from those reflected in these forward-looking statements and the differences could be substantial. We disclaim any obligation to update these forward-looking statements or disclose any difference, except as may be required by securities laws, between our actual results and those reflected in these statements. Although we believe that our plans, intentions and expectations reflected in or suggested by the forward-looking statements in this report are reasonable, we can give no assurance that such plans, intentions or expectations will be achieved. The terms "HUGHES Telematics," "we," "us" and "our" refer to the business, operations and financial results of HUGHES Telematics, Inc.

Overview

We are a telematics services company that provides a suite of real-time voice and data communications services and applications. These services and applications are enabled through a state-of-the-art communications center designed with flexibility to connect various mobile devices with content, services and call centers. Within the automotive industry, our communications center allows for two way voice and data communications to vehicles and supports, among other things, critical safety and security services as well as location-based services and remote diagnostics. Since November 16, 2009, we have been the exclusive telematics services provider in the United States for all new vehicles sold by Mercedes-Benz, and we are now the preferred provider of telematics services for all Mercedes-Benz vehicles purchased prior to November 16, 2009. These services are marketed under the mbrace brand. In addition, our In-Drive solution offers services to consumers or other third parties through an aftermarket hardware device that we have developed and which we intend to distribute through relationships with companies and organizations with large customer or membership bases for installation in existing vehicles.

Through our wholly-owned subsidiary, Networkfleet, we currently offer remote vehicle monitoring and other data services with sales generated through a combination of distribution arrangements with large fleet management service providers, a network of resellers and direct sales. Networkfleet's service offerings are enabled by an aftermarket hardware device that is sold by Networkfleet for installation in vehicles. Owners and operators of a fleet of vehicles use these services to monitor driver performance for unauthorized or unsafe vehicle usage, as well as analyze data such as the current location of a vehicle, fuel consumption, mileage, emissions status and diagnostic trouble codes.

On May 12, 2010, we entered into the LLC Agreement with Qualcomm, a leader in developing and delivering innovative digital wireless communications products and services, and AMAC, a healthcare communications company dedicated to the provision of support services to the healthcare community, forming Lifecomm. Lifecomm intends to design, develop, finance and operate a mobile personal emergency response service which will permit subscribers to initiate requests for emergency assistance services through a wearable device that is able to communicate information to and support voice interactions between the subscriber and an emergency assistance call center. Lifecomm expects to launch its service offerings in the fourth

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quarter of 2011.

On August 30, 2010, we entered into an agreement with a large insurance company to provide our In-Drive telematics services to certain customers of the insurance company. Pursuant to the agreement, we will configure our telematics platform to support the program and provide our aftermarket hardware device to the insurance company's customers to enable the delivery of telematics services to the insurance company and the insurance company's customers. In addition, we will be responsible for, among other things, certain website development to allow the insurance company's customers to access program information and maintenance and support of the hardware devices, including warranty. Pursuant to the agreement and subject to fulfillment of our obligations thereunder, we will receive minimum aggregate payments from the insurance company of approximately \$24.1 million in the first two years of the contract for the configuration of our telematics platform to support the program, development of the program website, the final testing and deployment of the hardware device, other program launch activities and the procurement by us of an agreed upon minimum number of hardware devices which we will provide to the insurance company's customers. During the year ended December 31, 2010 and the three months ended March 31, 2011, we received approximately \$5.5 million and \$2.9 million, respectively, of such amounts, and we expect to receive an additional \$12.1 million during the remainder of the year ending December 31, 2011 and the remaining balance in the year ending December 31, 2012. In addition, we expect to receive recurring payments from the insurance company's customers subject to and in connection with their subscription to the offered telematics services. We expect to launch our service to the insurance company's customers and begin revenue generating activities in the third quarter of 2011.

Selected Segment Data

We classify our operations into three principal business segments: (i) the HUGHES Telematics segment, which provides the telematics solution which is being marketed to automakers and other parties and includes the operations relating to our contract with Mercedes-Benz and our In-Drive product offering; (ii) the Networkfleet segment, which provides an aftermarket wireless fleet management solution targeted to the local fleet market; and (iii) the Lifecomm segment, which is developing and will operate a mobile personal emergency response service which will permit subscribers to initiate requests for emergency assistance services through a wearable device. The following tables set forth revenues and (loss) income from operations by operating segment:

	Three Months Ended March 31,	
	2011	2010
	(in thousands)	
Revenues:		
HUGHES Telematics	\$ 6,541	\$ 21
Networkfleet	9,422	8,146
Lifecomm	—	—
Total	\$ 15,963	\$ 8,167
(Loss) Income from operations:		
HUGHES Telematics	\$ (14,518)	\$ (17,777)
Networkfleet	293	311
Lifecomm	(2,051)	—
Total	\$ (16,276)	\$ (17,466)

Results of Operations for the Three Months Ended March 31, 2011 Compared to the Three Months Ended March 31, 2010

Revenues

Service revenues relate to the consideration received from the provision of Networkfleet's monitoring and tracking services and of the mbrace services to owners and lessees of Mercedes-Benz vehicles and are recognized as revenue when earned over the applicable subscription term. Hardware revenues consist principally of the sale of Networkfleet's telematics device. The following table sets forth information related to revenue for the three months ended March 31, 2011 and 2010:

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	Three Months Ended March 31,	
	2011	2010
	(in thousands)	
Services	\$13,601	\$6,056
Hardware	2,362	2,111
Total revenues	\$15,963	\$8,167

Total revenues for the three months ended March 31, 2011 increased to approximately \$16.0 million, a 95% increase from the approximately \$8.2 million of total revenues for the three months ended March 31, 2010. This increase was primarily due to an approximately \$6.5 million of service revenues recognized related to the mbrace service offering in the three months ended March 31, 2011 compared to less than \$0.1 million of revenues recognized in the three months ended March 31, 2010 and an approximately \$1.0 million, or 17% , increase in Networkfleet's service revenues in the three months ended March 31, 2011 compared to the three months ended March 31, 2010. Units active on Networkfleet's network increased to approximately 119,000 as of March 31, 2011, a 13% increase from the approximately 105,000 units active as of March 31, 2010. Service revenues are expected to continue to increase in future periods as (i) we continue to earn the deferred revenue related to the provision of services to paying subscribers of the mbrace service, (ii) we convert additional mbrace subscribers from a trial to a paid subscription, (iii) we transition paying subscribers from the Mercedes-Benz service formerly marketed as Tele Aid to our service platform and (iv) Networkfleet continues to sell additional hardware devices thereby growing the number of active units on its network. Further, we expect to begin generating revenue from our In-Drive service offering beginning in the third quarter of 2011 and from our Lifecomm service offering in the fourth quarter of 2011.

Hardware revenues for the three months ended March 31, 2011 increased by approximately \$0.3 million as compared to the three months ended March 31, 2010 due primarily to an increase in the number of units sold from approximately 6,500 units in the three months ended March 31, 2010 to approximately 7,600 units in the three months ended March 31, 2011, an increase of 17%.

Cost of Revenues

Cost of services includes per-unit monthly charges from various wireless, mapping and roadside assistance providers and the salaries and related benefits for employees who support the call centers and manage the data centers. Cost of hardware sold consists primarily of the cost of direct materials required to produce Networkfleet's telematics device and the cost of shipping and installing devices. The following table sets forth information related to costs of revenue for the three months ended March 31, 2011 and 2010:

	Three Months Ended March 31,	
	2011	2010
	(in thousands)	
Cost of services	\$ 5,867	\$ 5,228
Cost of hardware		

Weighted average number of shares:

Weighted average number of shares used in calculating basic earnings per share

2011	29,612
2010	29,265

Effect of dilutive stock-based compensation plans:

Stock options	-	369
Long-term incentive plan	-	38

Weighted average number of shares used in calculating diluted earnings per share

2011	29,612
2010	29,672

Average market price of common stock used

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for calculation of dilutive shares	\$ 34.89	\$ 33.88
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Net (loss)/income per share:

Basic	(\$0.05)	\$ 0.32
Diluted	(\$0.05)	\$ 0.31

As of March 31, 2008 and 2007, there was no dilution resulting from the convertible debt instrument, purchased call option, and warrant that are described in Note 11.

For the three months ended March 31, 2008, the Company has excluded 356,000 potentially dilutive shares from its calculation of diluted earnings per share because to do so would have been antidilutive.

The following table presents the number of shares issued and outstanding:

	Class A Shares	Class B Shares	Less: Treasury Shares	Net shares Outstanding
December 31, 2007	34,865,744	3,236,098	(8,530,066)	29,571,776
March 31, 2008	34,974,850	3,236,098	(8,530,066)	29,680,882

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9. Inventories

Inventories consist of the following:

(in thousands)	March 31, 2008	December 31, 2007
Finished goods	\$ 119,993	\$ 119,141
Work in process	62,472	67,374
Raw material and supplies	53,736	60,528
Total inventories	\$ 236,201	\$ 247,043

Inventories are stated at the lower of cost or market and are valued at average cost, net of reserves. The Company records a provision for obsolete inventory based on the age and category of the inventories.

10. Goodwill and other Intangible Assets

The Company accounts for goodwill and other intangible assets under the provisions of Statement of Financial Accounting Standards No. 142 (FAS 142), Goodwill and Other Intangible Assets. FAS No. 142 requires that goodwill and intangible assets with indefinite useful lives no longer be amortized, but instead tested for impairment at least annually.

The Company performs the test for goodwill impairment during the second quarter of each year. As a result of the test performed in the second quarter of 2007, no impairment provision was required. Goodwill and other long-lived assets are reviewed for impairment whenever events, such as significant changes in the business climate, plant closures, changes in product offerings, or other circumstances indicate that the carrying amount may not be recoverable.

The Company is continuing to amortize certain patents, trade names, customer contracts and technology assets that have finite lives. For purposes of applying FAS 142, the Company has determined that the reporting units are the Americas, Europe, and Asia Pacific businesses within the Paper Machine Clothing segment, the Albany Doors segment, the Engineered Fabrics segment, and the Engineered Composites segment. Fair values of the reporting units and the related implied fair values of their respective goodwill were established using public company analysis and discounted cash flows.

The changes in intangible assets and goodwill from December 31, 2007 to March 31, 2008, were as follows:

(in thousands)	Balance at December 31, 2007	Amortization	Currency translation	Balance at March 31, 2008
Amortized intangible assets:				
Patents	\$ 2,091	(\$126)	\$ 147	\$ 2,112
Trade names	2,044	(188)	128	1,984
Customer contracts	6,693	(264)	-	6,429
Technology	389	(11)	-	378
Total amortized intangible assets	\$ 11,217	(\$589)	\$ 275	\$ 10,903
Unamortized intangible assets:				
Goodwill	\$ 194,660	\$ -	\$ 11,892	\$ 206,552

As of March 31, 2008, goodwill included \$141,514,000 in the Paper Machine Clothing segment, \$38,940,000 in the Albany Door Systems segment, \$20,136,000 in the Engineered Fabrics segment, and \$5,962,000 in the Engineered Composites segment.

Estimated amortization expense of intangibles for the years ending December 31, 2008 through 2012 is as follows:

Year	Annual amortization (in thousands)
2008	\$ 2,636
2009	2,469
2010	1,833
2011	1,372
2012	865
	\$ 9,175

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11. Financial Instruments

Long term debt consists of the following:

(in thousands)	March 31, 2008	December 31, 2007
Convertible notes issued in March 2006 with fixed interest rates of 2.25%, due in year 2026	\$ 180,000	\$ 180,000
Private placement with a fixed interest rate of 5.34%, due in years 2013 through 2017	150,000	150,000
April 2006 credit agreement with borrowings outstanding at an average interest rate of 3.77%.	142,000	116,000
Various notes and mortgages relative to operations principally outside the United States, at an average rate of 4.99% in 2008 and 5.80% in 2007 due in varying amounts through 2021	246	1,015
Industrial revenue financings at an average interest rate of 1.75% in 2008 and 1.75% in 2007, due in varying amounts through 2009	471	564
Long term debt	\$ 472,717	447,579

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Less: current portion	(386)	(1,146)
Long term debt, net of current portion	\$ 472,331	\$ 446,433

The weighted average rate for all debt was 3.76% as of March 31, 2008 and 4.06% as of December 31, 2007.

In October 2005, the Company entered into a Note Agreement and Guaranty (the Prudential Agreement) with the Prudential Insurance Company of America, and certain other purchasers, in an aggregate principal amount of \$150,000,000. The notes bear interest at a rate of 5.34% and have a maturity date of October 25, 2017, with mandatory prepayments of \$50,000,000 on October 25, 2013 and October 25, 2015. At the noteholders election, certain prepayments may also be required in connection with certain asset dispositions or financings. The notes may not otherwise be prepaid without a premium, under certain market conditions. The Note Agreement contains customary terms, as well as affirmative covenants, negative covenants and events of default comparable to those in the Company s current principal revolving credit facility. For disclosure purposes, we are required to measure the fair value of outstanding debt on a recurring basis.

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The fair value of the note agreement was approximately \$158,855,000, which was measured using active market interest rates.

In March 2006, the Company issued \$180,000,000 principal amount of 2.25% convertible notes. The notes are convertible upon the occurrence of specified events and at any time on or after February 15, 2013, into cash up to the principal amount of notes converted and shares of the Company s Class A common stock with respect to the remainder, if any, of the Company s conversion obligation at a conversion rate of 22.487 shares per \$1,000 principal amount of notes (equivalent to a conversion price of \$44.47 per share of Class A common stock). The fair value of the convertible notes was approximately \$172,350,000, which was measured using quoted prices in active markets.

In connection with the offering, the Company has entered into convertible note hedge and warrant transactions with respect to its Class A common stock at a net cost of \$14,700,000. These transactions are intended to reduce the potential dilution upon conversion of the notes by providing the Company with the option, subject to certain exceptions, to acquire shares which offset the delivery of newly issued shares upon conversion of the notes.

Emerging Issues Task Force (EITF) Issue No. 00-19, Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company s Own Stock , (EITF 00-19) provides guidance for distinguishing between permanent equity, temporary equity and assets and liabilities. The convertible feature of the notes, the convertible note hedge, and the warrant transactions each meet the requirements of EITF 00-19 to be accounted for as equity instruments. As such, the convertible feature of the notes has not been accounted for as a derivative (which would be marked to market each reporting period) and in the event the debt is converted, no gain or loss is recognized, as the cash payment of principal reduces the recorded liability and the issuance of common shares would be recorded in stockholders equity.

In addition, the amount paid for the call option and the premium received for the warrant were recorded as additional paid-in capital in the accompanying consolidated balance sheet and are not accounted for as derivatives (which would be marked to market each reporting period). Incremental net shares for the convertible note feature and the warrant agreement will be included in future diluted earnings per share calculations for those periods in which the Company s average common stock price exceeds \$44.47 per share in the case of the Senior Notes and \$52.16 per share in the case of the warrants. The purchased call option is anti-dilutive and is excluded from the diluted earnings per share

calculation.

On April 14, 2006, the Company entered into a \$460,000,000 five-year revolving credit agreement (the "Credit Agreement"), under which \$142,000,000 was outstanding as of March 31, 2008. The applicable interest rate for borrowings under the agreement is LIBOR plus a spread, based on the Company's leverage ratio at the time of borrowing. The agreement includes covenants that could limit the Company's ability to purchase Common Stock, pay dividends, acquire other companies or dispose of its assets.

Reflecting, in each case, the effect of subsequent amendments to each agreement, the Company is required to maintain a leverage ratio of not greater than 3.50 to 1.00 under the Credit Agreement, and a leverage ratio of not greater than 3.00 to 1.00 (or 3.50 to 1.00 for a period of six fiscal quarters following a material acquisition, as defined) under the Prudential Agreement. The Company is also required to maintain minimum interest coverage of 3.00 to 1.00 under each agreement. As of March 31, 2008, the Company's leverage ratio under the agreement was 2.82 to 1.00 and the interest coverage ratio was 7.64 to 1.00. The Company may purchase its Common Stock or pay dividends to the extent its leverage ratio remains at or below 3.00 to 1.00, and may make acquisitions provided its leverage ratio would not exceed 3.00 to 1.00 after giving pro forma effect to the acquisition. The Company's ability to borrow additional amounts under the credit agreement is

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conditional upon the absence of any defaults, as well as the absence of any material adverse change. Based on the maximum leverage ratio and the Company's consolidated EBITDA (as defined in the agreement), and without modification to any other credit agreements as of March 31, 2008, the Company would have been able to borrow an additional \$25,000,000 under its loan agreements.

On December 10, 2007, the Company and Bank of America entered into a US dollar-to-euro cross-currency and interest rate swap agreement with a notional value of \$150,000,000. The Company has designated the swap to be an effective hedge of its euro net asset exposure relating to European operations. Under the swap agreement, the Company has notionally exchanged \$150,000,000 at a fixed interest rate of 5.34% for euro 101,951,000 at a fixed interest rate of 5.28%. The exchange was executed at an exchange rate of 1.4713 US dollars per euro. The majority of the cash flows in the swap agreement are aligned with the Company's principal and interest payment obligations on its \$150,000,000, Prudential Agreement. The final maturity of the swap matches the final maturity of the Prudential Agreement.

The Company's swap agreement qualifies as a hedge of net investments in foreign operations under the provisions of FAS No. 133, "Accounting for Derivative Instruments and Hedging Activities". Under FAS No. 133, changes in fair value of derivatives that qualify as hedges are recorded in shareholders' equity, net of tax, in the caption "Derivative valuation adjustments". As of March 31, 2008, the fair value of the swap agreement was a liability \$7,327,000, which was measured using current exchange rates and discounted cash flows. The liability was recorded in other noncurrent liabilities. Of that amount, \$2,873,000 was included in deferred taxes and the remaining \$4,454,000 was included in shareholders' equity.

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12. Contingencies

Albany International Corp. (Albany) is a defendant in suits brought in various courts in the United States by plaintiffs who allege that they have suffered personal injury as a result of exposure to asbestos-containing products previously manufactured by Albany. Albany produced asbestos-containing paper machine clothing synthetic dryer fabrics marketed during the period from 1967 to 1976 and used in certain paper mills. Such fabrics generally had a useful life of three to twelve months.

Albany was defending against 18,529 claims as of May 2, 2008. This compares with 18,789 such claims as of February 1, 2008, 18,791 claims as of October 19, 2007, 18,813 claims as of July 27, 2007, 19,120 claims as of April 27, 2007, 19,388 claims as of February 16, 2007, 19,416 claims as of December 31, 2006, 19,283 claims as of October 27, 2006, 24,451 claims as of December 31, 2005, 29,411 claims as of December 31, 2004, 28,838 claims as of December 31, 2003, 22,593 claims as of December 31, 2002, 7,347 claims as of December 31, 2001, 1,997 claims as of December 31, 2000, and 2,276 claims as of December 31, 1999. These suits allege a variety of lung and other diseases based on alleged exposure to products previously manufactured by Albany.

Albany anticipates that additional claims will be filed against it and related companies in the future, but is unable to predict the number and timing of such future claims. These suits typically involve claims against from twenty to more than two hundred defendants, and the complaints usually fail to identify the plaintiffs work history or the nature of the plaintiffs alleged exposure to Albany s products. Pleadings and discovery responses in those cases in which work histories have been provided indicate claimants with paper mill exposure in less than 10% of total claims reported, and only a portion of those claimants have alleged time spent in a paper mill to which Albany is believed to have supplied asbestos-containing products.

As of May 2, 2008, approximately 12,440 of the claims pending against Albany are pending in Mississippi. Of these, approximately 11,871 are in federal court, at the multidistrict litigation panel (MDL), either through removal or original jurisdiction. (In addition to the 11,871 Mississippi claims pending against the Company at the MDL, there are approximately 888 claims pending against the Company at the MDL removed from various United States District Courts in other states.)

On May 31, 2007 the MDL issued an administrative order that required each MDL plaintiff to provide detailed information regarding, among other things, the alleged asbestos-related medical diagnoses. The order does not require exposure information with this initial filing. The first set of plaintiffs were required to submit their filings with the Court by August 1, 2007, with deadlines for additional sets of plaintiffs monthly thereafter until December 1, 2007, by which time all MDL plaintiffs were to have filed compliant reports. The process, however, remains incomplete, as a number of extensions have been requested and granted, and reports continue to be filed. The order states that the Court may dismiss the claims of any plaintiff who fails to comply, but no such action has yet been taken.

Because the order of the MDL does not require the submission of alleged exposure information, the Company cannot predict if any dismissals will result from these initial filings. The MDL will at some point begin conducting settlement conferences, at which time the plaintiffs will be required to submit short position statements setting forth exposure information. The Company does not expect the MDL to begin the process of scheduling the settlement conference for several months. Consequently, the Company believes that the effects of the new order will not be fully known or realized for some time.

Based on past experience, communications from certain plaintiffs counsel, and the advice of the Company s Mississippi counsel, the Company expects the percentage of Mississippi claimants able to demonstrate time spent in a paper mill to which Albany supplied asbestos-containing products during a period in which Albany s

asbestos-containing products were in use to be considerably lower than the total number of pending claims. However, due to the large number of inactive claims pending in the MDL and the lack of alleged exposure information, the Company does not believe a meaningful estimate can be made regarding the range of possible loss with respect to these remaining claims.

It is the position of Albany and the other paper machine clothing defendants that there was insufficient exposure to asbestos from any paper machine clothing products to cause asbestos-related injury to any plaintiff. Furthermore, asbestos contained in Albany's synthetic products was encapsulated in a resin-coated yarn woven into the interior of the fabric, further reducing the likelihood of fiber release. While the Company believes it has meritorious defenses to these claims, it has settled certain of these cases for amounts it considers reasonable given the facts and circumstances of each case. The Company's insurer, Liberty Mutual, has defended each case and funded settlements under a standard reservation of rights. As of May 2, 2008, the Company had resolved, by means of settlement or dismissal, 21,878 claims. The total cost of resolving all claims was \$6,748,000. Of this amount, \$6,713,000, or 99%, was paid by the Company's insurance carrier. The Company has approximately \$130 million in confirmed insurance coverage that should be available with respect to current and future asbestos claims, as well as additional insurance coverage that it should be able to access.

Brandon Drying Fabrics, Inc.

Brandon Drying Fabrics, Inc. (Brandon), a subsidiary of Geschmay Corp., which is a subsidiary of the Company, is also a separate defendant in many of the asbestos cases in which Albany is named as a defendant. Brandon was defending against 8,689 claims as of May 2, 2008. This compares with 8,741 such claims as of February 1, 2008 and October 19, 2007, 9,023 claims as of July 27, 2007, 9,089 claims as of April 27, 2007, 9,189 claims as of February 16, 2007, 9,114 claims as of December 31, 2006, 8,992 claims as of October 27, 2006, 9,566 claims as of December 31, 2005, 9,985 claims as of December 31, 2004, 10,242 claims as of December 31, 2003, 11,802 claims as of December 31, 2002, 8,759 claims as of December 31, 2001, 3,598 claims as of December 31, 2000, and 1,887 claims as of December 31, 1999. The Company acquired Geschmay Corp., formerly known as Wangner Systems Corporation, in 1999. Brandon is a wholly-owned subsidiary of Geschmay Corp. In 1978, Brandon acquired certain assets from Abney Mills (Abney), a South Carolina textile manufacturer. Among the assets acquired by Brandon from Abney were assets of Abney's wholly-owned subsidiary, Brandon Sales, Inc. which had sold, among other things, dryer fabrics containing asbestos made by its parent, Abney. It is believed that Abney ceased production of asbestos-containing fabrics prior to the 1978 transaction. Although Brandon manufactured and sold dryer fabrics under its own name subsequent to the asset purchase, none of such fabrics contained asbestos. Under the terms of the Assets Purchase Agreement between Brandon and Abney, Abney agreed to indemnify, defend, and hold Brandon harmless from any actions or claims on account of products manufactured by Abney and its related corporations prior to the date of the sale, whether or not the product was sold subsequent to the date of the sale. It appears that Abney has since been dissolved. Nevertheless, a representative of Abney has been notified of the pendency of these actions and demand has been made that it assume the defense of these actions. Because Brandon did not manufacture asbestos-containing products, and because it does not believe that it was the legal successor to, or otherwise responsible for obligations of Abney with respect to products manufactured by Abney, it believes it has strong defenses to the claims that have been asserted against it. In some instances, plaintiffs have voluntarily dismissed claims against it, while in others it has entered into what it considers to be reasonable settlements. As of May 2, 2008, Brandon has resolved, by means of settlement or dismissal, 8,883 claims for a total of \$152,499. Brandon's insurance carriers initially agreed to pay 88.2% of the total indemnification and defense costs related to these proceedings, subject to the standard reservation of rights. The remaining 11.8% of the costs had been borne directly by Brandon. During 2004, Brandon's insurance carriers agreed to cover 100% of indemnification and defense costs, subject to policy limits and the standard reservation of rights, and to reimburse Brandon for all indemnity and defense costs paid directly by Brandon related to these proceedings.

Mount Vernon

In some of these asbestos cases, the Company is named both as a direct defendant and as the successor in interest to Mount Vernon Mills (Mount Vernon). The Company acquired certain assets from Mount Vernon in 1993. Certain plaintiffs allege injury caused by asbestos-containing products alleged to have been sold by Mount Vernon many years prior to this acquisition. Mount Vernon is contractually obligated to indemnify the Company against any liability arising out of such products. The Company denies any liability for products sold by Mount Vernon prior to the acquisition of the Mount Vernon assets. Pursuant to its contractual indemnification obligations, Mount Vernon has assumed the defense of these claims. On this basis, the Company has successfully moved for dismissal in a number of actions.

While the Company does not believe, based on currently available information and for the reasons stated above, that a meaningful estimate of a range of possible loss can be made with respect to such claims, based on its understanding of the insurance policies available, how settlement amounts have been allocated to various policies, its recent settlement experience, the absence of any judgments against the Company or Brandon, the ratio of paper mill claims to total claims filed, and the defenses available, the Company currently does not anticipate any material liability relating to the resolution of the aforementioned pending proceedings in excess of existing insurance limits. Consequently, the Company currently does not anticipate, based on currently available information, that the ultimate resolution of the aforementioned proceedings will have a material adverse effect on the financial position, results of operations or cash flows of the Company. Although the Company cannot predict the number and timing of future claims, based on the foregoing factors and the trends in claims against it to date, the Company does not anticipate that additional claims likely to be filed against it in the future will have a material adverse effect on its financial position, results of operations, or cash flows. The Company is aware that litigation is inherently uncertain, especially when the outcome is dependent primarily on determinations of factual matters to be made by juries. The Company is also aware that numerous other defendants in asbestos cases, as well as others who claim to have knowledge and expertise on the subject, have found it difficult to anticipate the outcome of asbestos litigation, the volume of future asbestos claims, and the anticipated settlement values of those claims. For these reasons, there can be no assurance that the foregoing conclusions will not change.

21**13. Changes in Stockholders' Equity**

The following table summarizes changes in Stockholders' Equity:

(in thousands)	Class A Common Stock	Class B Common Stock	Additional paid in capital	Retained earnings	Accumulated items of other comprehensive income	Treasury stock	Total Shareholders' Equity
December 31, 2007	\$ 35	\$ 3	\$ 326,608	\$ 544,228	(\$12,180)	(\$259,023)	\$ 599,671
Net (loss)				(1,492)			(1,492)
Shares contributed to ESOP			2,544				2,544

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Proceeds from options exercised		354		354
Dividends declared		(3,259)		(3,259)
Stock option expense		42		42
Tax benefit of options exercised		74		74
Issuance of shares under long-term incentive plan		624		624
Change in derivative valuation adjustment			(6,019)	(6,019)
Amortization and adjustment of pension liability			(2,694)	(2,694)
Cumulative translation adjustment/other			36,333	36,333
March 31, 2008	\$	35 \$	3 \$ 330,246 \$	539,477 \$ 15,440 (\$259,023) \$ 626,178

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14. Comprehensive Income

Comprehensive income consists of the following:

(in thousands)	Three Months Ended	
	March 31, 2008	2007
Net (loss)/income	(\$1,492)	\$ 9,305
Other comprehensive income, before tax:		
Foreign currency translation adjustments	36,333	4,517
Amortization of pension liability adjustment	371	(815)
Pension and postretirement liability adjustments	(4,742)	
Derivative valuation adjustment	(9,893)	-
Income taxes related to items of other comprehensive income:		
Amortization of pension liability adjustment	(145)	318
Pension and postretirement liability adjustments	1,822	-
Derivative valuation adjustment	3,874	-
Other comprehensive income, net of tax	27,620	4,020

Comprehensive income	\$	26,128	\$	13,325
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15. Recent Accounting Pronouncements

In September 2006, the FASB issued FAS No. 157, Fair Value Measurements (FAS No. 157). FAS No. 157 clarifies the principle that fair value should be based on the assumptions market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. The Company's adoption of this Standard on January 1, 2008 did not have a material effect on its financial statements.

In February 2007, the FASB issued FAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115 (FAS No. 159). FAS No. 159 provides companies with a choice to measure certain financial assets and liabilities at fair value that are not currently required to be measured at fair value (the Fair Value Option). Election of the Fair Value Option is made on an instrument-by-instrument basis and is irrevocable. The Company's adoption of this Standard on January 1, 2008 did not have a material effect on its financial statements.

In December 2007, the FASB issued FAS No. 160 Noncontrolling Interests in Consolidated Financial Statements an amendment to ARB No. 51. FAS 160 establishes accounting and reporting standards that require the ownership interest in subsidiaries held by parties other than the parent be clearly identified and presented in the consolidated balance sheets within equity, but separate from the parent's equity; the amount of consolidated net income attributable to the parent and the noncontrolling interest be clearly identified and presented on the face of the consolidated statement of earnings; and changes in a parent's ownership interest while the parent retains its controlling financial interest in its subsidiary be accounted for consistently. This statement is effective for fiscal years beginning on or after December 15, 2008. The Company does not expect the adoption of FAS No. 160 to have a material effect on its financial statements.

In December 2007, the FASB issued Statement of Financial Accounting Standards ("FAS") No. 141 (revised 2007), Business Combinations ("FAS 141(R)" which replaces FAS No. 141, Business Combinations. FAS 141(R) retains the underlying concepts of FAS 141 in that all business combinations are still required to be accounted for at fair value under the acquisition method of accounting but FAS 141(R) changed the method of applying the acquisition method in a number of significant aspects. FAS 141(R) is effective on a prospective basis for all business combinations for which the acquisition date is on or after the beginning of the first annual period subsequent to December 15, 2008, with the exception of the accounting for valuation allowances on deferred taxes and acquired tax contingencies. FAS 141(R) amends FAS 109 such that adjustments made to valuation allowances on deferred taxes and acquired tax contingencies associated with acquisitions that closed prior to the effective date of FAS 141(R) would also apply the provisions of FAS 141(R). Early adoption is not allowed. We are currently evaluating the effects, if any, that FAS 141(R) may have on our financial statements, but the Company does not expect the adoption of FAS No. 141(R) to have a material effect on its financial statements.

In March 2008, the FASB issued FAS No. 161, Disclosures about Derivative Instruments and Hedging Activities. The Standard requires enhanced disclosures about derivative instruments and is effective for fiscal periods beginning after November 15, 2008. The Company does not expect adoption of this Standard to have a material effect on its financial statements.

16. Subsequent events

On April 10, 2008, the Company announced its plans to shut down its Mansfield, Massachusetts facility and consolidate its technical and manufacturing operations there into other facilities in Europe and North America.

On May 4, 2008, the Company announced that it has entered into an agreement to sell its Filtration Technologies business, which is based primarily in Gosford, Australia, and Zhangjiagang, China for \$45,000,000, subject to contractual closing adjustments.

On May 4, 2008, the Company announced a general downsizing of its remaining operations in Australia. While the operation will continue to support the Australia and New Zealand markets for paper machine clothing, and the global market for Fiber Cement, production of press felts will be scaled back. Production of high performance doors in Australia will cease.

Given local legal requirements and discussions with employees affected, the Company cannot presently determine the amount of expense to be incurred for severance and termination payments related to these actions. As a result, the Company is not yet able to estimate total charges to be incurred in connection with these planned actions. The estimated charges, and related cash expenditures, are expected to be incurred during the remainder of 2008.

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

The following Management's Discussion and Analysis (MD&A) is intended to help the reader understand the results of operations and financial condition of the Company. The MD&A is provided as a supplement to, and should be read in conjunction with, the Consolidated Financial Statements and the accompanying Notes.

Overview

Albany International Corp. (the Registrant, the Company, or we) and its subsidiaries are engaged in five business segments.

The Paper Machine Clothing segment includes fabrics and belts used in the manufacture of paper and paperboard (PMC or paper machine clothing). The Company designs, manufactures, and markets paper machine clothing for each section of the paper machine. It manufactures and sells more paper machine clothing worldwide than any other company. PMC consists of large permeable and non-permeable continuous belts of

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custom-designed and custom-manufactured engineered fabrics that are installed on paper machines and carry the paper stock through each stage of the paper production process. PMC products are consumable products of technologically sophisticated design that utilize polymeric materials in a complex structure. The design and material composition of PMC can have a considerable effect on the quality of paper products produced and the efficiency of the paper machines on which it is used. Principal products in the PMC segment include forming, pressing and dryer fabrics, and process belts. A forming fabric assists in sheet formation and conveys the very dilute sheet through the section. Press fabrics are designed to carry the sheet through the presses, where water pressed from the sheet is carried through the press nip in the fabric. In the dryer section, dryer fabrics manage air movement and hold the sheet against heated cylinders to enhance drying. Process belts are used in the press section to increase dryness and enhance sheet properties, as well as in other sections of the machine to improve runnability and enhance sheet qualities. The Company's customers in the PMC segment are paper industry companies, some of which operate in multiple regions of the world. The Company's manufacturing processes and distribution channels for PMC are substantially the same in each region of the world in which it operates.

Albany Door Systems (ADS) designs, manufactures, sells, and services high-speed, high-performance industrial doors worldwide, for a wide range of interior, exterior, and machine protection industrial applications. Already a high performance door leader, ADS further expanded its market position in North America with the second-quarter 2007 acquisition of the assets and business of R-Bac Industries, the fastest-growing high-performance door company in North America, whose product lines are complementary to Albany's. The business segment also derives revenue from aftermarket sales and service.

The Company's other reportable segments are emerging businesses that apply the Company's core competencies in advanced textiles and materials to other industries, including specialty materials and composite structures for aircraft and other applications (Albany Engineered Composites); a variety of products similar to PMC for application in the corrugators, pulp, nonwovens, building products, tannery and textile industries (Albany Engineered Fabrics); and insulation for outdoor clothing, gloves, footwear, sleeping bags and home furnishings (PrimaLoft® Products). No class of similar products or services within these segments accounted for 10% or more of the Company's consolidated net sales in any of the past three years.

Trends

The Company's primary segment, Paper Machine Clothing, accounted for approximately 70% of consolidated revenues during 2007. Paper machine clothing is purchased primarily by manufacturers of paper and paperboard. According to data published by RISI, Inc., world paper and paperboard production volumes have grown at an annual rate of approximately 2.6% over the last ten years. Based on data from RISI, demand for paper is expected to grow approximately 2.9% over the next five years. The paper and paperboard industry has been characterized by an evolving but essentially stable manufacturing technology based on the wet-forming papermaking process. This process, of which paper machine clothing is an integral element, requires a very large capital investment. Consequently, management does not believe that a commercially feasible substitute technology to paper machine clothing is likely to be developed and

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incorporated into the paper production process by paper manufacturers in the foreseeable future. For this reason, management expects that demand for paper machine clothing will continue into the foreseeable future.

The world paper and paperboard industry tends to be cyclical, with periods of healthy paper prices followed by increases in new capacity, which then leads to increased production and higher inventories of paper and paperboard, followed by a period of price competition and reduced

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profitability among the Company's customers. Although sales of paper machine clothing do not tend to be as cyclical, the Company may experience somewhat greater demand during periods of increased production and somewhat reduced demand during periods of lesser production.

The world paper and paperboard industry experienced a significant period of consolidation and rationalization from approximately 2000 through 2004. While significant consolidation among paper and paperboard suppliers slowed after 2004, machine closures, or announcements of additional machine closures, continued during 2005, 2006 and 2007 in North America as well as Europe. During this period, a number of older, less efficient machines in areas where significant established capacity existed were closed or were the subject of planned closure announcements, while at the same time a number of newer, faster and more efficient machines began production or plans for the installation of such newer machines were announced in areas of growing demand for paper and paperboard (such as Asia and South America). Management anticipates that this trend is likely to continue in the near term.

At the same time, technological advances in paper machine clothing, while contributing to the papermaking efficiency of customers, have lengthened the useful life of many of the Company's products and reduced the number of pieces required to produce the same volume of paper. As the Company introduces new value creating products and services, it is often able to charge higher prices or increase market share in certain areas as a result of these improvements. However, increased prices and share have not always been sufficient to offset completely a decrease in the number of fabrics sold.

The factors described above result in a steady decline in the number of pieces of paper machine clothing, while the average fabric size is increasing. The net effect of these trends is that the specific volume of paper machine clothing consumption (measured in kilograms or square meters) has been increasing at a rate of approximately 1% per year over the past several years.

During 2006, the Company reported that price competition in Western Europe had an adverse impact on the Company's operating results in this segment. In the third and fourth quarters of 2006, and in the first two quarters of 2007, sales of paper machine clothing to customers in Western Europe were significantly lower than the same quarter of the previous year. This also contributed to reduced operating income within this segment, as well as overall operating income, during those quarters.

The Company's response to that pricing disruption has been to initiate a deliberate, intensive three-year process of restructuring and performance improvement initiatives. In the mature paper machine clothing markets of North America and Europe, the Company is driving for growth in market share, while the Company is positioning itself to expand in the rapidly growing markets of Asia and South America. At the same time that the Company is adjusting its manufacturing footprint to align with these regional markets, management is taking actions to reduce costs significantly. Additionally, the Company has reorganized its PMC research and product development function resulting in better ability to bring value-added products to market faster.

The Albany Door Systems segment derives most of its revenue from the sale of high-performance doors, particularly to customers in Europe. The purchase of these doors is normally a capital expenditure item for customers and, as such, market opportunities tend to fluctuate with industrial capital spending. If economic conditions weaken, customers may reduce levels of capital expenditures, which could have a negative effect on sales and earnings in the Albany Door Systems segment. The large amount of revenue derived from sales and manufacturing outside the United States could cause the reported financial results for the Albany Door Systems segment to be more sensitive than the other segments of the Company to changes in currency rates.

The Engineered Fabrics segment derives its revenue from various industries that use fabrics and belts for industrial applications other than the manufacture of paper and paperboard. Approximately 40% of revenue in this segment is derived from sales to the nonwovens industry, which includes the manufacture of diapers, personal care and household

wipes, and fiberglass-reinforced roofing shingles. Segment sales in the European and Pacific regions combined are almost at the same level as sales within the Americas.

The Engineered Composites segment (AEC) serves primarily the aerospace industry, with custom-designed composite and advanced composite parts for static and dynamic applications. Management believes AEC has the potential to grow at least 35% per annum for the next five years and has the potential to become a second core business of the Company. AEC has experienced significant growth in net sales during the last few years, due both to the introduction of new products as well as growth in demand and application for previously existing products. The principal challenges and opportunities in this segment involve managing this growth opportunity.

The PrimaLoft® Products segment includes sales of insulation for outdoor clothing, gloves, footwear, sleeping bags, and home furnishings. The segment has manufacturing and sales operations in the United States, Europe, and Asia.

Foreign Currency

Albany International operates in many geographic regions of the world and has more than half of its business in countries outside the United States. A substantial portion of the Company's sales are denominated in euros or other currencies. In some locations, the profitability of transactions is affected by the fact that sales are denominated in a currency different from the currency in which the costs to manufacture and distribute the products are denominated. As a result, changes in the relative values of U.S. dollars, euros and other currencies affect revenues and profits as the results are translated into U.S. dollars in the consolidated financial statements.

From time to time, the Company enters into foreign currency or other derivative contracts in order to enhance cash flows or to mitigate volatility in the financial statements that can be caused by changes in currency exchange rates.

Review of Operations

2008 vs. 2007

On May 4, 2008, the Company announced that it had entered into an agreement to sell its Filtration Technologies business for \$45 million, subject to contractual closing adjustments. Filtration Technologies' principal operations are in Gosford, Australia, and Zhangjiagang, China. In the first quarter of 2008, net sales were \$10.5 million, an increase of 47% compared to the first quarter of 2007. The activities of this business are reported as a discontinued operation in the first-quarter financial statements and accordingly are excluded from Tables 1, 2, and 3, below.

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In the first quarter of 2008, the Company modified its reportable segments to be consistent with changes in the Company's organizational structure. Prior year data has been modified to conform to the current year presentation. The Company has filed a Form 8-K with reclassified segment data for quarters ending in 2007, as well as annual data for 2006 and 2007.

Net sales from continuing operations increased \$22.6 million to \$273.2 million, or 9.0 percent compared to the same period last year. Excluding the effect of changes in currency translation rates, net sales increased 1.3 percent. The following table, which reflects changes in the Company's reportable segments, presents net sales and the effect of changes in currency translation rates:

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Table 1

(in thousands)	Net Sales Three Months ended March 31,		Percent Change	Impact of Changes in Currency Translation Rates	Percent Change excluding Currency Rate Effect
	2008	2007			
Paper Machine Clothing	\$183,015	\$178,631	2.5%	\$11,946	-4.2%
Albany Door Systems	45,132	34,494	30.8%	5,082	16.1%
Engineered Fabrics	28,110	25,531	10.1%	2,280	1.2%
Engineered Composites	11,088	7,775	42.6%	-	42.6%
PrimaLoft® Products	5,863	4,183	40.2%	110	37.5%
Total	\$273,208	\$250,614	9.0%	\$19,418	1.3%

Gross profit was 34.7 percent of net sales in the first quarter of 2008, compared to 38.6 percent in the same period of 2007. The difference is principally due to decreases in PMC net sales, particularly in North America, and costs associated with performance-improvement initiatives.

Selling, technical, general, and research (STG&R) expenses were 30.2 percent of net sales in the first quarter of 2008 compared to 29.4 percent in the first quarter of 2007. STG&R expenses were \$82.4 million in the first quarter of 2008, in comparison to \$73.7 million in the first quarter of 2007. First-quarter 2008 STG&R expenses included \$5.8 million related to the effect of changes in currency translation rates and \$5.1 million of expenses related to performance-improvement initiatives. First-quarter 2007 STG&R expenses included \$1.6 million related to performance-improvement initiatives.

Operating income was \$7.2 million in the first quarter of 2008, compared to \$15.5 million for the same period of 2007. The following table presents segment operating income:

Table 2

(in thousands)	Operating Income Three Months ended March 31,	
	2008	2007
Paper Machine Clothing	\$18,550	\$26,542

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Albany Door Systems	2,836	1,732
Engineered Fabrics	5,569	4,424
Engineered Composites	(1,826)	(615)
Primaloft® Products	1,078	510
Research expenses	(5,871)	(5,011)
Unallocated expenses	(13,156)	(12,061)
Total	\$7,180	\$15,521

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First-quarter segment operating income included the following expenses associated with restructuring and performance-improvement initiatives:

Table 3

(in thousands)	2008			2007	
	Restructuring and Other, Net	Idle-capacity Costs at Plants Closing	Performance-improvement Initiatives	Total	Restructuring and Performance-improvement Initiatives
Paper Machine Clothing	\$6,402	\$684	\$3,323	\$10,409	\$6,846
Albany Door Systems	-	-	135	135	-
Unallocated expenses	(1,040)	-	3,948	2,908	2,469
Total	\$5,362	\$684	\$7,406	\$13,452	\$9,315

The first-quarter 2008 net restructuring charges of \$5.4 million (\$0.14 per share) were principally due to costs associated with the closure of the Company's Montgomery, Alabama, plant that was announced in the first quarter of 2008 and other restructuring activities. In addition, idle-capacity costs of \$0.7 million, related to previously announced plant closures, and \$7.4 million of expenses related to ongoing performance-improvement initiatives increased cost of goods sold by \$3.0 million (\$0.08 per share), and STG&R expenses by \$5.1 million (\$0.14 per share). The increased STG&R expenses are principally due to the non-capitalized portion of SAP project costs, costs related to the implementation of the global procurement initiative, and termination costs. Cost of goods sold during the quarter includes additional costs related to the start-up of the greenfield PMC plant in China and equipment relocation expenses. Performance-improvement costs in the first quarter of 2007 amounted to \$1.7 million, of which \$1.6 million was included in STG&R expenses.

Research expenses increased \$0.9 million principally due to increased development efforts in the Engineered Composites business. Unallocated expenses increased \$1.1 million principally due to higher costs associated with restructuring and performance improvement initiatives.

Interest expense increased to \$4.3 million for the first quarter of 2008, compared to \$3.3 million for 2007. The increase in 2008 reflects higher average levels of debt outstanding in 2008.

The effective first-quarter income tax rate before discrete tax items was 20 percent in 2008 and 25 percent in 2007. Included in first-quarter 2008 income tax expense are discrete tax adjustments that decreased net income by \$0.13 per share.

Net loss per share for the first quarter of 2008 was \$0.05, after reductions of \$0.36 from net restructuring charges, idle capacity costs related to restructuring, and costs related to continuing performance-improvement initiatives. Discrete income tax adjustments reduced net income by \$0.13 per share. Net income per share for the first quarter of 2007 was \$0.32, after expenses related to restructuring and performance improvement initiatives reduced net income per share by \$0.24.

Paper Machine Clothing Segment

Compared to the first quarter of 2007, trade sales in the Americas region declined 8.3 percent. Trade sales in South America increased 10.5 percent, while sales in North America declined 12.9 percent. Volume in North America was negatively affected by paper mill closures, reduced capacity utilization rates in some paper grades, and longer running life of paper machine clothing.

Orders in the Americas region during the quarter were 14.7 percent ahead of very strong first-quarter 2007 orders. Cost-reduction activities in North America are proceeding on schedule. Headcount has dropped 9 percent compared to the first quarter of 2007, and lower costs are beginning to become apparent in lower average production costs in finished goods inventories.

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In Western Europe, compared to the first quarter of 2007, trade sales in euros declined 5.8 percent due to lower sales volume and lower average prices. While prices were lower than the first quarter of 2007, they were relatively stable compared to recent quarters and based on current orders are likely to remain stable for the rest of the year. While volume was lower than in the first quarter of 2007, reflecting a weakened European paper industry, market share increased and orders are strong. Restructuring activities in Europe have resulted in a 13 percent reduction in headcount, which nearly offset the effect of lower sales.

Trade sales in the Pacific region were 9.9 percent higher than the first quarter of 2007. Orders are strong and the new capacity in Asia is beginning to come on stream as planned.

First-quarter gross profit as a percentage of net sales was 37.4% for 2008 compared to 42.0% for 2007. The difference was principally due to decreases in net sales, particularly in North America, and costs associated with performance-improvement initiatives. First-quarter operating income was \$18.6 million for 2008, compared to \$26.5 million for 2007. Segment expenses for restructuring and performance improvement initiatives increased \$3.5 million.

Albany Door Systems Segment

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Trade sales in Europe in euros were up 13.8 percent, and orders were up 10.5 percent compared to the first quarter of 2007. Much of this increase was due to strong product sales. Compared to last year, operating margins improved due to the 2007 consolidation of European manufacturing operations.

In North America, trade sales increased 33.7 percent and orders increased 39.0 percent compared to the same period last year. Most of this increase was due to the second-quarter 2007 R-Bac acquisition. Sales were negatively affected by the construction slowdown in the U.S.

First-quarter gross profit as a percentage of net sales was 32.7% for 2008 compared to 33.5% for 2007. The difference reflects a higher portion of segment sales in 2008 that were generated by initial product sales. First-quarter operating income increased from \$1.7 million in 2007 to \$2.8 million in 2008 principally due to the effect of higher sales.

Engineered Fabrics Segment

Excluding the effect of changes in currency translation rates, net sales compared to the first quarter of 2007 increased 1.2 percent. Sales in the North American building products market were negatively affected by the downturn in the U.S. economy and the related decline in new construction. Some of the weakness in this area has been offset by growth in sales to Asia.

First-quarter gross profit as a percentage of net sales was 39.9% for 2008 compared to 37.7% for 2007. First-quarter operating income increased to \$5.6 million in 2008, compared to \$4.4 million in 2007. The improvement in 2008 reflects increased efficiencies in Europe and the new facility in Kaukauna, Wisconsin.

Engineered Composites Segment

Net sales increased to \$11.1 million in the first quarter of 2008, compared to \$7.8 million in the first quarter of 2007, an increase of 42.6%.

As expected, the Engineered Composites segment generated an operating loss of \$1.8 million during the quarter, but by late in the quarter showed significant improvement in operating efficiencies.

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PrimaLoft® Products Segment

Net sales increased 40.2 percent compared to the same period last year. While outerwear sales in North America and Europe showed good growth, home furnishings sales in North America were down significantly due to weakness in the retail market.

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First-quarter gross profit as a percentage of net sales was 47.2% for 2008 compared to 46.7% for 2007. First-quarter operating income increased from \$0.5 million in 2007 to \$1.1 million in 2008. The improvement in 2008 was principally due to higher sales.

Liquidity and Capital Resources

On May 4, 2008, the Company announced that it has agreed to sell its filtration business, which manufactures filtration products for a variety of industrial processes, most notably power generation. The Company has reached the point in the growth of its emerging businesses when management is starting to make choices in how it allocates capital among them. While the filtration business has very appealing growth prospects, its basis for competitive advantage, and thus for sustainable profitable growth, is not tightly connected to Albany's core competencies. The Company will use the proceeds of the sale to fund planned capital expenditures outside of the U.S. and for general working capital purposes.

Net cash provided by operating activities was \$7.4 million in the first quarter of 2008, compared to \$17.3 million for the same period of 2007. Capital spending during the first quarter of 2008 was \$31.6 million. The Company expects capital spending in 2008 to be approximately \$140 million, and continues to expect that capital spending in 2009 will be approximately \$70 million. Depreciation and amortization were \$14.8 million and \$1.2 million, respectively, for the first quarter of 2008. Depreciation and amortization are estimated to be \$68 million and \$7 million for 2008, and \$72 million and \$10 million for 2009.

The Company finances its business activities primarily with cash generated from operations and borrowings, primarily under \$180 million of 2.25% convertible notes issued in March 2006, \$150 million of 5.34% long-term indebtedness to Prudential Capital Group issued in October 2005, and its revolving credit agreement as described in Notes to Consolidated Financial Statements. Company subsidiaries outside of the United States may also maintain working capital lines with local banks, but borrowings under such local facilities tend not to be significant.

The effective first-quarter income tax rate on continuing operations before discrete tax items was 20% in 2008 and 25% in 2007. The Company currently anticipates its consolidated effective tax rate on continuing operations in 2008 will not exceed 20% before any discrete items, although there can be no assurance that this will not change.

Under Trends, management discussed certain recent trends in its paper machine clothing segment that have had a negative impact on demand for the Company's products within that segment, as well as its strategy for addressing these trends. Management also discussed pricing competition within this segment and the negative effect of such competition on segment sales and earnings. If these trends continue or intensify, and if management's strategy for addressing them should prove inadequate, the Company's operating cash flow could be adversely affected. In any event, although historical cash flows may not, for all of these reasons, necessarily be indicative of future cash flows, the Company expects to continue to be able to generate substantial cash from sales of its products and services in future periods.

In October 2005, the Company closed on a \$150 million borrowing from Prudential Capital Group. The principal is due in three installments of \$50 million each in 2013, 2015, and 2017 (an average life of 10 years), and the interest rate is fixed at 5.34 percent. Proceeds from the borrowing were used to pay down all \$127 million of floating-rate indebtedness at the time outstanding under the Company's existing credit facility. Under this agreement the Company is required to maintain a leverage ratio of not greater than 3.00 to 1.00 and a minimum interest coverage of at least 3.00 to 1.00. As of March 31, 2008, the Company's leverage ratio under the agreement was 2.82 to 1.00 and the interest coverage ratio was 7.64 to

1.00. The Company may purchase its Common Stock or pay dividends to the extent its leverage ratio remains at or below 3.00 to 1.00, and may make acquisitions provided its leverage ratio would not exceed 3.00 to 1.00 after giving pro forma effect to the acquisition. The Company's ability to borrow additional amounts under the credit agreement is conditional upon the absence of any defaults, as well as the absence of any material adverse change. Based on the maximum leverage ratio and the Company's consolidated EBITDA (as defined in the agreement), and without modification to any other credit agreements as of March 31, 2008, the Company would have been able to borrow an additional \$25 million under the loan agreement. There are cross-default provisions in this agreement whereby a default under the borrowing from the five-year revolving credit agreement would trigger a default under this agreement.

In March 2006, the Company issued \$180 million principal amount of 2.25% convertible notes. The notes are convertible upon the occurrence of specified events and at any time on or after February 15, 2013, into cash up to the principal amount of notes converted and shares of the Company's Class A common stock with respect to the remainder, if any, of the Company's conversion obligation at an initial conversion rate of 22.462 shares per \$1,000 principal amount of notes (equivalent to an initial conversion price of \$44.52 per share of Class A common stock).

In connection with the offering, the Company entered into convertible note hedge and warrant transactions with respect to its Class A common stock at a net cost of \$14.7 million. These transactions are intended to reduce the potential dilution upon conversion of the notes by providing the Company with the option, subject to certain exceptions, to acquire shares that offset the delivery of newly issued shares upon conversion of the notes.

On April 14, 2006, the Company entered into a new \$460 million five-year revolving credit agreement, under which \$142 million was outstanding as of March 31, 2008. The agreement replaced a similar \$460 million revolving credit facility. Under the terms of the new agreement, commitment fees on the unused portion of the facility were reduced from 0.25% to 0.09% and the term was extended from 2009 to 2011. The applicable interest rate for borrowings under the new agreement, as well as under the old agreement, is LIBOR plus a spread, based on the Company's leverage ratio at the time of borrowing. As of March 31, 2008, the interest rate under this agreement was 3.77%. Spreads under the new agreement are 15 to 50 basis points lower than under the old agreement. The new agreement includes covenants similar to the old agreement, which could limit the Company's ability to purchase Common Stock, pay dividends, or acquire other companies or dispose of its assets. The Company is also required to maintain a leverage ratio of not greater than 3.00 to 1.00 and a minimum interest coverage of at least 3.00 to 1.00. As of March 31, 2008, the Company's leverage ratio under the agreement was 2.82 to 1.00 and the interest coverage ratio was 7.64 to 1.00. The Company may purchase its Common Stock or pay dividends to the extent its leverage ratio remains at or below 3.00 to 1.00, and may make acquisitions provided its leverage ratio would not exceed 3.00 to 1.00 after giving pro forma effect to the acquisition. The Company's ability to borrow additional amounts under the credit agreement is conditional upon the absence of any defaults, as well as the absence of any material adverse change. Based on the maximum leverage ratio and the Company's consolidated EBITDA (as defined in the agreement), and without modification to any other credit agreements as of March 31, 2008, the Company would have been able to borrow an additional \$25 million under the loan agreement. There are cross-default provisions in this agreement whereby a default under the borrowing from Prudential would trigger a default under this agreement.

On December 10, 2007, the Company and Bank of America entered into a US dollar-to-euro cross-currency and interest rate swap agreement with a notional value of \$150,000,000. The Company has designed the swap to be an effective hedge of its euro net asset exposure relating to European operations. Under the swap agreement, the Company has notionally exchanged \$150,000,000 at a fixed interest rate of 5.34% for euro 101,950,700 at a fixed interest rate of 5.28%. The exchange was executed at an exchange rate of 1.4713 US dollars per euro. The majority of the cash flows in the swap agreement are aligned with the Company's principal and interest payment obligations on its \$150,000,000 Prudential Agreement. The final maturity of the swap matches the final maturity of the Prudential Agreement.

The Company's swap agreement qualifies as a hedge of net investments in foreign operations under the provisions of FAS No. 133, Accounting for Derivative Instruments and Hedging Activities. Under FAS No. 133, changes in fair value of derivatives that qualify as hedges are recorded in shareholders' equity, net of tax, in the caption Derivative valuation adjustment. As of March 31, 2008, the fair value of the swap agreement

was a liability \$7,327,000, which was recorded

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in other noncurrent liabilities. Of that amount, \$2,873,000 was included in deferred taxes and the remaining \$4,454,000 was included in shareholders' equity.

Dividends have been declared each quarter since the fourth quarter of 2001, and first-quarter dividends per share were \$0.11 in 2008 and \$0.10 in 2007. Decisions with respect to whether a dividend will be paid, and the amount of the dividend, are made by the Board of Directors each quarter. To the extent the Board declares cash dividends in the future, the Company would expect to pay such dividends out of operating cash flow. Future cash dividends will be dependent on debt covenants and on the Board's assessment of the Company's ability to generate sufficient cash flows.

In August 2006, the Company announced that the Board of Directors authorized management to purchase up to 2 million additional shares of its Class A Common Stock. The Board's action authorizes management to purchase shares from time to time, in the open market or otherwise, whenever it believes such purchase to be advantageous to the Company's shareholders, and it is otherwise legally permitted to do so. As of March 31, 2008, no share purchases had been made under the 2006 authorization.

Outlook

First quarter 2008 results were depressed by a slowdown in each of the Company's North American operations, except for Engineered Composites. By far the largest effect was in PMC. Despite continuing strength in market share, the successful conclusion of several important contract negotiations in 2007, and unusually strong orders, sales in North America were down 12.9 percent compared to the same period in 2007. This decline in sales reduced operating income by an estimated \$3.5 million. There are a number of reasons for this decline, the most significant of which was the impact of the general economic slowdown on an already weakened paper industry. In most publication grades, paper mill operating rates dropped well below their 2007 levels. At the same time, some mills ran their paper machine clothing longer than is customary. The net effect was lower consumption of paper machine clothing. The weakness in PMC sales was most pronounced in the third month of the quarter, just as it was in the fourth quarter of 2007.

Management saw further evidence of this economic weakness in sales of Engineered Fabrics to the U.S. building products and fiber cement industries, sales of PrimaLoft® products to the U.S. home furnishings retail market, and sales of doors to some construction-sensitive market segments in the U.S.

Apart from this economic weakness in North America, there were no significant deviations from management's expectations for the first quarter. Each of the emerging businesses performed to plan. Albany Engineered Composites increased net sales by 43 percent compared to the first quarter of 2007, made excellent progress in manufacturing efficiencies, and continues on trend toward becoming profitable in the third quarter of 2008. Fueled by continuing growth in the European market, Albany Doors had another strong quarter in both sales and orders; and Engineered Fabrics was strong across the board, except for its North American construction-oriented product lines.

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The three-year process of internal restructuring, launched in the third quarter of 2006 continued on plan, with the announced closures of the Mansfield, Massachusetts, and Montgomery, Alabama, operations. The effects of this process are beginning to become apparent: combined headcount in North American and European PMC is down 11 percent; gross margins are increasing in the PMC product lines where the most significant restructuring has taken place dryers in the Americas and press in Europe; and average cost of finished goods inventories in those product lines is declining. Meanwhile, several new products in the R&D pipeline are approaching market trials, or had successful initial trials during the quarter; the expansions in Asia and South America remain on schedule; and the Company is progressing toward the toughest and most important milestone in our SAP implementation, the July 2008 go-live for the North American PMC and Engineered Fabrics operations. The Company thus remains on trend toward the strong cash generation that it has been projecting for 2009.

Looking forward to the second quarter and the balance of the year, the economic slowdown in North America, coupled with the possibility of a European slowdown later in the year, adds an element of uncertainty to the short-term outlook. Orders are strong across each of the Company's businesses. Market share in PMC is strong and getting stronger, and based on current orders, management expects PMC pricing to be stable in Europe through the rest of 2008. And even though the increases in oil prices are putting upward pressure on materials costs, management expects to mitigate the effect of those increases through the balance of the year. With all of these positive factors at work, management would

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ordinarily be optimistic about the prospects for the next few quarters. But the continuing economic weakness in North America tempers management's optimism about the short-term outlook.

Non-GAAP Measures

This Form 10-Q contains certain items, such as sales excluding currency effects, and consolidated net income and consolidated and segment operating income excluding costs associated with restructuring and performance-improvement initiatives, that may be considered to be non-GAAP financial measures. Such items are provided because management believes that, when presented together with the GAAP items to which they relate, they can provide additional useful information to investors regarding the registrant's financial condition, results of operations, and cash flows. Presenting increases or decreases in sales, after currency effects are excluded, can give managements and investors insight into underlying sales trends. An understanding of the impact in a particular quarter of specific restructuring and performance-improvement measures, and in particular of the costs associated with the implementation of such measures, on the Company's net income or operating income, or the operating income of a business segment, can give management and investors additional insight into quarterly performance, especially when compared to quarters in which such measures had a greater or lesser effect, or no effect. The effect of changes in currency translation rates is calculated by converting amounts reported in local currencies into U.S. dollars at the exchange rate of a prior period. That amount is then compared to the U.S. dollar amount reported in the current period.

Recent Accounting Pronouncements

In September 2006, the FASB issued FAS No.157, Fair Value Measurements (FAS No. 157). FAS No. 157 clarifies the principle that fair value should be based on the assumptions market participants would use when pricing an asset or liability and establishes a fair value hierarchy that prioritizes the information used to develop those assumptions. The Company's adoption of this Standard on January 1, 2008 did not have a material effect on its financial statements.

In February 2007, the FASB issued FAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115 (FAS No. 159)*. FAS No. 159 provides companies with a choice to measure certain financial assets and liabilities at fair value that are not currently required to be measured at fair value (the *Fair Value Option*). Election of the Fair Value Option is made on an instrument-by-instrument basis and is irrevocable. The Company's adoption of this Standard on January 1, 2008 did not have a material effect on its financial statements.

In December 2007, the FASB issued FAS No. 160 *Noncontrolling Interests in Consolidated Financial Statements* an amendment to ARB No. 51. FAS 160 establishes accounting and reporting standards that require the ownership interest in subsidiaries held by parties other than the parent be clearly identified and presented in the consolidated balance sheets within equity, but separate from the parent's equity; the amount of consolidated net income attributable to the parent and the noncontrolling interest be clearly identified and presented on the face of the consolidated statement of earnings; and changes in a parent's ownership interest while the parent retains its controlling financial interest in its subsidiary be accounted for consistently. This statement is effective for fiscal years beginning on or after December 15, 2008. The Company does not expect the adoption of FAS No. 160 to have a material effect on its financial statements.

In December 2007, the FASB issued Statement of Financial Accounting Standards (FAS) No. 141 (revised 2007), *Business Combinations* FAS 141(R) which replaces FAS No. 141, *Business Combinations*. FAS 141(R) retains the underlying concepts of FAS 141 in that all business combinations are still required to be accounted for at fair value under the acquisition method of accounting but FAS 141(R) changed the method of applying the acquisition method in a number of significant aspects. FAS 141(R) is effective on a prospective basis for all business combinations for which the acquisition date is on or after the beginning of the first annual period subsequent to December 15, 2008, with the exception of the accounting for valuation allowances on deferred taxes and acquired tax contingencies. FAS 141(R) amends FAS 109 such that adjustments made to valuation allowances on deferred taxes and acquired tax contingencies associated with acquisitions that closed prior to the effective date of FAS 141(R) would also apply the provisions of FAS 141(R). Early adoption is not allowed. We are currently evaluating the effects, if any, that FAS 141(R) may have on our financial statements, but the Company does not expect the adoption of FAS No. 141(R) to have a material effect on its financial statements.

In March 2008, the FASB issued FAS No. 161, *Disclosures about Derivative Instruments and Hedging Activities*. The Standard requires enhanced disclosures about derivative instruments and is effective for fiscal periods beginning after November 15, 2008. The Company does not expect adoption of this Standard to have a material effect on its financial statements.

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Critical Accounting Policies and Assumptions

The following should be read in conjunction with the Consolidated Financial Statements and Notes thereto.

The Company's discussion and analysis of its financial condition and results of operations are based on the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP). The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities.

The Company records sales when persuasive evidence of an arrangement exists, delivery has occurred, the selling price is fixed, and collectibility is reasonably assured. The timing of revenue recognition is dependent upon the contractual arrangement between the Company and its customers. These arrangements, which may include provisions for transfer of title and guarantees of workmanship, are specific to each customer. Sales contracts in the Albany Door Systems segment may include product and installation services. For these sales, the Company applies the provisions of EITF 00-21, Revenue Arrangements with Multiple Deliverables. The Company's contracts that include product and installation services generally do not qualify as separate units of accounting and, accordingly, revenue for the entire contract value is recognized upon completion of installation services. The Company limits the concentration of credit risk in receivables by closely monitoring credit and collection policies. The Company records allowances for sales returns as a deduction in the computation of net sales. Such provisions are recorded on the basis of written communication with customers and/or historical experience.

The Company maintains allowances for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. If the financial condition of the Company's customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

Goodwill and other long-lived assets are reviewed for impairment whenever events such as significant changes in the business climate, plant closures, changes in product offerings, or other circumstances indicate that the carrying amount may not be recoverable. The Company performs a test for goodwill impairment at least annually. The determination of whether these assets are impaired involves significant judgments based on short and long-term projections of future performance. Changes in strategy and/or market conditions may result in adjustments to recorded asset balances.

The Company has investments in other companies that are accounted for under the equity method of accounting. Investments accounted for under the equity method are included in Investments in associated companies. The Company performs regular reviews of the financial condition of the investees to determine if its investment is impaired. If the financial condition of the investees were to no longer support their valuations, the Company would record an impairment provision.

The Company has pension and postretirement benefit costs and liabilities that are developed from actuarial valuations. Inherent in these valuations are key assumptions, including discount rates and expected return on plan assets, which are updated on an annual basis. The Company is required to consider current market conditions, including changes in interest rates, in making these assumptions. Changes in the related pension and postretirement benefit costs or credits may occur in the future due to changes in the assumptions. The amount of annual pension plan funding and annual expense is subject to many variables, including the investment return on pension plan assets and interest rates. Assumptions used for determining pension plan liabilities and expenses are evaluated and updated at least annually. The largest benefit plans are the U.S. pension plan and the U.S. postretirement benefits plan, which account for 41% and 21% of the total company benefit obligations. Discount rate assumptions are based on the population of plan participants and a mixture of high-quality fixed income investments for which the average maturity approximates the average remaining service period of plan participants. The largest portion of pension plan assets (35% for the U.S. plan and 74% for non-U.S. plans) was invested in equities. The assumption for expected return on plan assets is based on historical and expected returns on various categories of plan assets. The U.S. plan accounts for 64% of the total consolidated pension plan assets. The benefit obligation was calculated using the RP-2000 Combined Healthy Mortality Table projected to 2015 using Scale AA with phase-out and without collar adjustment. Weakness in investment returns and low interest rates, or deviations in results from other assumptions, could result in the Company making equal or greater pension plan contributions in future years, as compared to 2007. Including anticipated contributions for all pension plans, the Company estimates that contributions will amount to approximately \$9.6 million. Actual contributions for 2007 totaled \$20.8 million. The

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Company adopted the provisions of FAS No. 158 in the fourth quarter of 2006, resulting in an increase of \$23.7 million in noncurrent deferred tax assets, a decrease of \$5.6 million in intangible assets, an increase of \$59.6 million in pension liabilities, and an increase of \$41.5 million in accumulated other comprehensive losses.

The Company records deferred income tax assets and liabilities for the tax consequences of differences between financial statement and tax bases of existing assets and liabilities. A tax valuation allowance is established, as needed, to reduce net deferred tax assets to the amount expected to be realized. In the event it becomes more likely than not that some or all of the deferred tax asset allowances will not be needed, the valuation allowance will be adjusted.

The Company has contingent liabilities for litigation, claims and assessments that result from the ordinary course of business. These matters are more fully described in Notes to the Consolidated Financial Statements.

Forward-looking statements

This quarterly report and the documents incorporated or deemed to be incorporated by reference in this quarterly report contain statements concerning our future results and performance and other matters that are forward-looking statements within the meaning of Section 27A of the Securities Act and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). The words believe, expect, anticipate, intend, plan, project, may, will and variations of such words or similar expressions are intended, but are not the exclusive means, to identify forward-looking statements. Because forward-looking statements are subject to risks and uncertainties, actual results may differ materially from those expressed or implied by the forward-looking statements.

There are a number of risks, uncertainties and other important factors that could cause actual results to differ materially from the forward-looking statements, including, but not limited to: changes in conditions in the industry in which the Company's Paper Machine Clothing segment competes or in the papermaking industry in general could change; failure to remain competitive in the industry in which the Company's Paper Machine Clothing segment competes; material and petroleum-related costs could increase more or faster than anticipated; failure to receive, or a delay in receiving, the benefits from the Company's capital expenditures and investments; the strategies described in this report to address certain business or operational matters could fail to be effective, or their effectiveness could be delayed; other risks and uncertainties detailed from time to time in the Company's filings with the SEC.

Further information concerning important factors that could cause actual events or results to be materially different from the forward-looking statements can be found in Industry Trends and Challenges, Risks and Opportunities sections of this quarterly report, as well as in the Risk Factors, section of the Company's most recent Annual Report on Form 10-K. Although the Company believes the expectations reflected in the Company's forward-looking statements are based upon reasonable assumptions, it is not possible to foresee or identify all factors that could have a material and negative impact on future performance. The forward-looking statements included or incorporated by reference in this quarterly report are made on the basis of management's assumptions and analyses, as of the time the statements are made, in light of their experience and perception of historical conditions, expected future developments and other factors believed to be appropriate under the circumstances.

Except as otherwise required by the federal securities laws, the Company disclaims any obligations or undertaking to publicly release any updates or revisions to any forward-looking statement contained or incorporated by reference in this report to reflect any change in the Company's expectations with regard thereto or any change in events, conditions or circumstances on which any such statement is based.

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Item 3. Quantitative and Qualitative Disclosures about Market Risk

For discussion of the Company's exposure to market risk, refer to Quantitative and Qualitative Disclosures About Market Risk under Item 7A of form 10-K, which is included as an exhibit to this Form 10-Q.

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Item 4. Controls and Procedures

(a) Disclosure controls and procedures.

The principal executive officers and principal financial officer, based on their evaluation of disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) as of the end of the period covered by this Quarterly Report on Form 10-Q, have concluded that the Company's disclosure controls and procedures are effective for ensuring that information required to be disclosed in the reports that it files or submits under the Securities Exchange Act of 1934 is recorded, processed, summarized and reported within the time periods specified in the Commission's rules and forms. Disclosure controls and procedures, include, without limitation, controls and procedures designed to ensure that information required to be disclosed in filed or submitted reports is accumulated and communicated to the Company's management, including its principal executive officer and principal financial officer as appropriate, to allow timely decisions regarding required disclosure.

(b) Changes in internal control over financial reporting.

There were no changes in the Company's internal control over financial reporting that occurred during the last fiscal quarter that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

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PART II OTHER INFORMATION

Item 1. LEGAL PROCEEDINGS

Albany International Corp. (Albany) is a defendant in suits brought in various courts in the United States by plaintiffs who allege that they have suffered personal injury as a result of exposure to asbestos-containing products previously manufactured by Albany. Albany produced asbestos-containing paper machine clothing synthetic dryer fabrics marketed during the period from 1967 to 1976 and used in certain paper mills. Such fabrics generally had a useful life of three to twelve months.

Albany was defending against 18,529 claims as of May 2, 2008. This compares with 18,789 such claims as of February 1, 2008, 18,791 claims as of October 19, 2007, 18,813 claims as of July 27, 2007, 19,120 claims as of April 27, 2007, 19,388 claims as of February 16, 2007, 19,416 claims as of December 31, 2006, 19,283 claims as of October 27, 2006, 24,451 claims as of December 31, 2005, 29,411 claims as of December 31, 2004, 28,838 claims as of December 31, 2003, 22,593 claims as of December 31, 2002, 7,347 claims as of December 31, 2001, 1,997 claims as of December 31, 2000, and 2,276 claims as of December 31, 1999. These suits allege a variety of lung and other diseases based on alleged exposure to products previously manufactured by Albany.

Albany anticipates that additional claims will be filed against it and related companies in the future, but is unable to predict the number and timing of such future claims. These suits typically involve claims against from twenty to more than two hundred defendants, and the complaints usually fail to identify the plaintiffs work history or the nature of the plaintiffs alleged exposure to Albany s products. Pleadings and discovery responses in those cases in which work histories have been provided indicate claimants with paper mill exposure in less than 10% of total claims reported, and only a portion of those claimants have alleged time spent in a paper mill to which Albany is believed to have supplied asbestos-containing products.

As of May 2, 2008, approximately 12,440 of the claims pending against Albany are pending in Mississippi. Of these, approximately 11,871 are in federal court, at the multidistrict litigation panel (MDL), either through removal or original jurisdiction. (In addition to the 11,871 Mississippi claims pending against the Company at the MDL, there are approximately 888 claims pending against the Company at the MDL removed from various United States District Courts in other states.)

On May 31, 2007 the MDL issued an administrative order that required each MDL plaintiff to provide detailed information regarding, among other things, the alleged asbestos-related medical diagnoses. The order does not require exposure information with this initial filing. The first set of plaintiffs were required to submit their filings with the Court by August 1, 2007, with deadlines for additional sets of plaintiffs monthly thereafter until December 1, 2007, by which time all MDL plaintiffs were to have filed compliant reports. The process, however, remains incomplete, as a number of extensions have been requested and granted, and reports continue to be filed. The order states that the Court may dismiss the claims of any plaintiff who fails to comply, but no such action has yet been taken.

Because the order of the MDL does not require the submission of alleged exposure information, the Company cannot predict if any dismissals will result from these initial filings. The MDL will at some point begin conducting settlement conferences, at which time the plaintiffs will be required to submit short position statements setting forth exposure information. The Company does not expect the MDL to begin the process of scheduling the settlement conference for several months. Consequently, the Company believes that the effects of the new order will not be fully known or realized for some time.

Based on past experience, communications from certain plaintiffs' counsel, and the advice of the Company's Mississippi counsel, the Company expects the percentage of Mississippi claimants able to demonstrate time spent in a paper mill to which Albany supplied asbestos-containing products during a period in which Albany's asbestos-containing products were in use to be considerably lower than the total number of pending claims. However, due to the large number of inactive claims pending in the MDL and the lack of alleged exposure information, the Company does not believe a meaningful estimate can be made regarding the range of possible loss with respect to these remaining claims.

It is the position of Albany and the other paper machine clothing defendants that there was insufficient exposure to asbestos from any paper machine clothing products to cause asbestos-related injury to any plaintiff. Furthermore, asbestos contained in Albany's synthetic products was encapsulated in a resin-coated yarn woven into the interior of the fabric, further reducing the likelihood of fiber release. While the Company believes it has meritorious defenses to these claims, it has settled certain of these cases for amounts it considers reasonable given the facts and circumstances of each case. The Company's insurer, Liberty Mutual, has defended each case and funded settlements under a standard reservation of rights. As of May 2, 2008, the Company had resolved, by means of settlement or dismissal, 21,878 claims. The total cost of resolving all claims was \$6,748,000. Of this amount, \$6,713,000, or 99%, was paid by the Company's insurance carrier. The Company has approximately \$130 million in confirmed insurance coverage that should be available with respect to current and future asbestos claims, as well as additional insurance coverage that it should be able to access.

Brandon Drying Fabrics, Inc.

Brandon Drying Fabrics, Inc. (Brandon), a subsidiary of Geschmay Corp., which is a subsidiary of the Company, is also a separate defendant in many of the asbestos cases in which Albany is named as a defendant. Brandon was defending against 8,689 claims as of May 2, 2008. This compares with 8,741 such claims as of February 1, 2008 and October 19, 2007, 9,023 claims as of July 27, 2007, 9,089 claims as of April 27, 2007, 9,189 claims as of February 16, 2007, 9,114 claims as of December 31, 2006, 8,992 claims as of October 27, 2006, 9,566 claims as of December 31, 2005, 9,985 claims as of December 31, 2004, 10,242 claims as of December 31, 2003, 11,802 claims as of December 31, 2002, 8,759 claims as of December 31, 2001, 3,598 claims as of December 31, 2000, and 1,887 claims as of December 31, 1999. The Company acquired Geschmay Corp., formerly known as Wangner Systems Corporation, in 1999. Brandon is a wholly-owned subsidiary of Geschmay Corp. In 1978, Brandon acquired certain assets from Abney Mills (Abney), a South Carolina textile manufacturer. Among the assets acquired by Brandon from Abney were assets of Abney's wholly-owned subsidiary, Brandon Sales, Inc. which had sold, among other things, dryer fabrics containing asbestos made by its parent, Abney. It is believed that Abney ceased production of asbestos-containing fabrics prior to the 1978 transaction. Although Brandon manufactured and sold dryer fabrics under its own name subsequent to the asset purchase, none of such fabrics contained asbestos. Under the terms of the Assets Purchase Agreement between Brandon and Abney, Abney agreed to indemnify, defend, and hold Brandon harmless from any actions or claims on account of products manufactured by Abney and its related corporations prior to the date of the sale, whether or not the product was sold subsequent to the date of the sale. It appears that Abney has since been dissolved. Nevertheless, a representative of Abney has been notified of the pendency of these actions and demand has been made that it assume the defense of these actions. Because Brandon did not manufacture asbestos-containing products, and because it does not believe that it was the legal successor to, or otherwise responsible for obligations of Abney with respect to products manufactured by Abney, it believes it has strong defenses to the claims that have been asserted against it. In some instances, plaintiffs have voluntarily dismissed claims against it, while in others it has entered into what it considers to be reasonable settlements. As of May 2, 2008, Brandon has resolved, by means of settlement or dismissal, 8,883 claims for a total of \$152,499. Brandon's insurance carriers initially agreed to pay 88.2% of the total indemnification and defense costs related to these proceedings, subject to the standard reservation of rights. The remaining 11.8% of the costs had been borne directly by Brandon. During 2004, Brandon's

Mount Vernon

In some of these asbestos cases, the Company is named both as a direct defendant and as the successor in interest to Mount Vernon Mills (Mount Vernon). The Company acquired certain assets from Mount Vernon in 1993. Certain plaintiffs allege injury caused by asbestos-containing products alleged to have been sold by Mount Vernon many years prior to this acquisition. Mount Vernon is contractually obligated to indemnify the Company against any liability arising out of such products. The Company denies any liability for products sold by Mount Vernon prior to the acquisition of the Mount Vernon assets. Pursuant to its contractual indemnification obligations, Mount Vernon has assumed the defense of these claims. On this basis, the Company has successfully moved for dismissal in a number of actions.

While the Company does not believe, based on currently available information and for the reasons stated above, that a meaningful estimate of a range of possible loss can be made with respect to such claims, based on its understanding of the insurance policies available, how settlement amounts have been allocated to various policies, its recent settlement experience, the absence of any judgments against the Company or Brandon, the ratio of paper mill claims to total claims filed, and the defenses available, the Company currently does not anticipate any material liability relating to the resolution of the aforementioned pending proceedings in excess of existing insurance limits. Consequently, the Company currently does not anticipate, based on currently available information, that the ultimate resolution of the aforementioned proceedings will have a material adverse effect on the financial position, results of operations or cash flows of the Company. Although the Company cannot predict the number and timing of future claims, based on the foregoing factors and the trends in claims against it to date, the Company does not anticipate that additional claims likely to be filed against it in the future will have a material adverse effect on its financial position, results of operations, or cash flows. The Company is aware that litigation is inherently uncertain, especially when the outcome is dependent primarily on determinations of factual matters to be made by juries. The Company is also aware that numerous other defendants in asbestos cases, as well as others who claim to have knowledge and expertise on the subject, have found it difficult to anticipate the outcome of asbestos litigation, the volume of future asbestos claims, and the anticipated settlement values of those claims. For these reasons, there can be no assurance that the foregoing conclusions will not change.

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Item 1A. Risk Factors.

There have been no material changes in risks since December 31, 2007. For discussion of risk factors, refer to Item 1A of the Company's Annual Report on Form 10-K for the year ended December 31, 2007.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

Management made no share purchases during the first quarter of 2008. Management remains authorized by the Board of Directors to purchase up to 2,000,000 shares of its Class A Common Stock.

Item 3. Defaults Upon Senior Securities
None

Item 4. Submission of Matters to a Vote of Security Holders
None

Item 5. Other Information
None

Item 6. Exhibits

Exhibit No.	Description
31.1	Certification of the Chief Executive Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Exchange Act.
31.2	Certification of the Chief Financial Officer pursuant to Rule 13a-14(a)/15d-14(a) of the Exchange Act.
32.1	Certification pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (Subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code)
99.1	Quantitative and qualitative disclosures about market risks as reported at December 31, 2007.

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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.

ALBANY INTERNATIONAL CORP.

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(Registrant)

Date: May 9, 2008

By /s/ Michael C. Nahl

Michael C. Nahl
Executive Vice President and Chief Financial Officer
(Principal Financial Officer)
