Zacks Small-Cap Research

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inTEST Corporation (INTT-NASDAQ)

INTT: Solid Quarter in Uncertain Times - OUTPERFORM

Current Recommendation	**Outperform**
Prior Recommendation	Neutral
Date of Last Change	02/23/2012
Current Price (08/01/12)	$3.30
Target Price	**$7.00**

OUTLOOK

inTEST Corporation is a designer, manufacturer and marketer of mechanical, thermal and electrical products that are used by semiconductor manufacturers in conjunction with automatic test equipment, (ATE), in the testing of integrated circuits, (ICs). Beyond its blue chip portfolio of semiconductor manufacturers, the firm has diversified into non-semi thermal testing products. This has the effect of diversifying revenues and opens the company up to new markets. In the test equipment world change is good; be it the broad switch to mobile computing, the march to finer geometries, or the growth of electronic content in automobiles more chip content means more testing for inTEST.

SUMMARY DATA

52-Week High	**$3.82**
52-Week Low	**$2.17**
One-Year Return (%)	**-3.51**
Beta	**1.31**
Average Daily Volume (sh)	**20,011**
Shares Outstanding (mil)	**10**
Market Capitalization ($mil)	**$34**
Short Interest Ratio (days)	**0.78**
Institutional Ownership (%)	**22**
Insider Ownership (%)	**20**
Annual Cash Dividend	**$0.00**
Dividend Yield (%)	**0.00**
5-Yr. Historical Growth Rates	
Sales (%)	**-0.4**
Earnings Per Share (%)	**N/A**
Dividend (%)	**N/A**
P/E using TTM EPS	**6.6**
P/E using 2012 Estimate	**10.6**
P/E using 2012 Estimate	**4.9**
Zacks Rank	**3**

Risk Level	**Moderate**
Type of Stock	**Small-Blend**
Industry	**Semiconductor-IC**

ZACKS ESTIMATES

Revenue
(in millions of $)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2010	9.5 A	15.3 A	11.3 A	10.1 A	46.2 A
2011	11.7 A	13.8 A	11.7 A	10.1 A	47.3 A
2012	10.7 A	13.6 A	10.0 E	12.0 E	46.3 E
2013					56.0 E

Earnings per Share
(EPS is operating earnings before non recurring items)

	Q1 (Mar)	Q2 (Jun)	Q3 (Sep)	Q4 (Dec)	Year (Dec)
2010	$0.11 A	$0.31 A	$0.17 A	$0.13 A	$0.72 A
2011	$0.13 A	$0.26 A	$0.22 A	$0.08 A	$0.70 A
2012	$0.07 A	$0.13 A	$0.02 E	$0.09 E	$0.31 E
2013					$0.68 E

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WHATS NEW

On August 1, 2012, inTest Corporation, reported financial results for its fiscal 2012 second quarter and six months, ended June 30, 2012.

Revenues during the second quarter of 2012 were $13.576 million compared to revenues of $10.731 million for the three months ended March 31, 2012 and revenues of $13.800 million during the second quarter ended June 30, 2011.

The Company's second quarter revenues marked the second consecutive quarter of revenue growth which was driven by increasing demand for mobility products and increased overall test capacity on the part of our customers.

Likewise, 14 percent of second quarter 2012 net revenues were derived from non-semiconductor test.

Over the last few years inTest has been transforming itself through the strategic diversification of its Thermal products segment.

As a result the Company now addresses growth markets in both the semiconductor and non-semiconductor areas, which include automotive, consumer electronics, defense aerospace, telecommunications and most recently the nuclear market.

inTest further reported that second quarter bookings were $11.8 million, down from its first quarter 2012 bookings of $12.9 million and from second quarter 2011 bookings of $13.5 million.

10 percent of the Company's second quarter 2012 bookings were derived from non-semiconductor test compared with 13 percent in the first quarter 2012.

Still, it should be noted that inTest's Thermal segment bookings increased 19 percent over its first quarter while segment sales increased nearly 7 percent over sales from the segment's first quarter.

The jump was due to a strong market in India and Korea during the quarter as India's year over year bookings increased by 136 and bookings for Korea in the second quarter were for more than in all of 2011.

While the second quarter Mechanical segment's bookings declined, segment sales increased 23% sequentially.

Furthermore, while the Company's Electrical segment is historically its smallest segment, it was the most profitable in both a quarterly and year to date period with sales improving 89 percent sequentially and the outlook for segment bookings for the third quarter remaining strong.

Gross margin during the second quarter improved to 45.6 percent compared to 42.8 percent from the first quarter fiscal 2012. However, gross margin fell from 49.3 percent for the three months ended June 30, 2011.

inTest reported second quarter 2012 net income of $1.334 million compared to a first quarter 2012 net loss of $43,000 and net income of $2.655 million for the three months ended June 30,2011.

The year over year drop in net income was primarily due to a year over year drop in gross margin as well

as a $582,000 increase in income tax expense in the second quarter of 2012 over the second quarter of 2011.

Similarly, first quarter 2012 results reflect the effect of approximately $696,000 in non-recurring costs related to the acquisition of Thermonics, Inc. on January 16, 2012 which include restructuring costs of $359,000 (related to facility closure costs) and acquisition related expenses of $337,000.

Based on a weighted average number of diluted shares outstanding of 10.360 million, diluted net income per share resulted in net income of $0.13 per share for the quarter. This compared to diluted net loss per share of $0.00 on a weighted average number of diluted shares of 10.205 million during the three months, ended March 31, 2012 and diluted net income per share of $0.26 on a weighted average number of diluted shares of 10.297 million during the second quarter ended June 30, 2011.

Revenues during the first half of 2012 were $24.307 million compared to revenues of $25.504 million for the six months ended June 30, 2011.

Gross margin during the first six months of 2012 dropped to 44.4 percent compared to 46.6 percent from the first half of fiscal 2011.

First half 2012 net income was $1.291 million compared to net income of $3.912 million for the six months ended June 30, 2011.

Here again, the year over year drop in net income was primarily due to the drop in gross margin and a $973,000 increase in total operating expenses as well as $494,000 increase in income tax expense in the first half 2012 compared to the first six months of 2011.

inTest's balance sheet improved sequentially during the second quarter with cash and equivalents of $11.699 million and working capital of $19.958 million. This compares to $10.101 million in cash and equivalents and working capital of $19.919 million for the period ended March 31, 2012.

Likewise, total stockholder's equity improved sequentially by roughly $1.354 million to $27.584 million.

Management anticipates that cash and equivalents will increase sequentially for the balance of 2012.

Still, as a result of current uncertainty in the global economic environment and analysts reducing their forecasts for 2012 CAPEX industry to now decline 10 to 15 percent, inTest stated that it's maintaining its fiscal discipline and cost controls.

Likewise, management continues to focus on leveraging its capabilities to serve its customers in its traditional semiconductor market and to further develop new markets addressed by inTEST Thermal Solutions.

Here again, over the past few years inTest has been attempting to transform itself through the strategic diversification of its Thermal Products segment, which remains the Company's strongest segment, driven by mobility and opportunities in the telecom market.

inTest expects to continue to leverage its Thermal division and the Sigma Systems acquisition and expects that non-semiconductor related products will continue to play an even greater role its future success as it further diversifies end market penetration.

Similarly, in January 2012, Temptronic Corporation, a member of inTEST Corporation's Thermal Solutions Group, closed on the acquisition of Thermonics, Inc.

With a purchase price for the assets of approximately $3.8 million in cash (which included net working capital of approximately $1.1 million) , Thermonics is expected to further enhance inTEST's presence in

the ATE industry as well as provide additional leverage into growth industries outside of the semiconductor industry.

Along the same lines, moving forward the Company expects non-semiconductor related products to play an even greater role in the Company's growth strategy and success.

Last, management reported that it anticipates that net revenues for the third quarter ended September 30, 2012 will be in the range of $9.5 to $10.5 million and that net earnings will be in the range of $0.00 to $0.04 per diluted share.

INVESTMENT THESIS

inTEST Corporation is a designer, manufacturer and marketer of mechanical, thermal and electrical products that are used by semiconductor manufacturers in conjunction with automatic test equipment, (ATE), in the testing of integrated circuits, (ICs). Beyond its blue chip portfolio of semiconductor manufacturers, the acquisition of Sigma has propelled the firm to diversify into non-semi thermal testing products. This has the effect of diversifying revenues and opens the company up to new markets. In the test equipment world change is good; be it the broad switch to mobile computing, the march to finer geometries, or the growth of electronic content in automobiles more chip content means more testing for inTEST.

Bullish signs

- **Complexity in chips increasing. As chips get smaller and more complex testing is more important.**
- **Chip content spread out over mobile phone, automobile, industrial goods rather than corporate IT.**
- **Non-semiconductor business has potential for growth as well as revenue diversification.**

Bearish Signs

- **More consumers in semiconductor than ever before. Pressure of macro economy weakness. (although many items price under $1,000.00)**
- **Firm is subject to the cyclical nature of the semiconductor equipment industry. Until non-semiconductor is large enough to offset.**

Focus on Thermal

The firm has built a diversified portfolio that includes non-semiconductor markets. This revenue should be a bit more inelastic and run on a different cyclical time frame than the semiconductor business. Non-semi revenue grew from 19% of total revenue ($9 Million) in 2010 to 29% of total revenue ($13 Million) in 2011. The firm’s goal is to grow Non-Semi revenue to 50% of revenue. The potential for Non-Semi is enormous because it incorporates any market that uses thermal.

inTEST is benefiting from the increasing need for temperature testing of circuit boards and specialized components.

The firm competes mainly on two levels.

- Wafer Level
- Discrete product Level

Wafer level is a solid business for the firm but will never be a significant growth engine. Standards in this area are not stringent and in the past 10 years prober manufacturers have taken over. inTEST serves smaller OEM's in this area with its Thermochuck product which tests semiconductor wafers at high and low (-65 to +400 C) temperatures at the wafer probing station.

The Discrete product level is where inTEST will experience growth over the next several years. These products provide the ability to characterize and stress test a variety of materials over extreme and variable temperature conditions that can occur in actual use.

The focus of is on four main areas solving unique and challenging temperature problems.

- Sensor Technology
- Fiber Optics
- Communication
- Defense and Aerospace

inTEST solves unique and challenging temperature problems.
Many of the thermal businesses the firm competes with are large companies that have standard products. The only model out there that has been in industrial thermal test to date is one where a customer must modify its test. inTEST's business model is quite the opposite. The company asks the question "what do you have to do to test?", and builds the equipment to fit the product. This is a model that's not generally been used out there because most of the companies they compete with are very large. Being small and able to move quickly, allows inTEST to win these custom jobs.

New Acquisition in Thermal
In January 2012, Temptronic Corporation, a member of inTEST Corporation's Thermal Solutions Group, closed on the acquisition of Thermonics, Inc. With a purchase price for the assets of approximately $3.8 million in cash (which included net working capital of approximately $1.1 million),Thermonics is expected to further enhance inTEST's presence in the ATE industry as well as provide additional leverage into growth industries outside of the semiconductor industry. The integration of the acquisition is on track and management expects it to be accretive to operations beginning in the second quarter of 2012. Furthermore, management anticipates a 30 percent net contribution margin on incremental revenues which are expected to improve sequentially throughout 2012 eventually reaching as much as 35 to 36 percent over time.

Real World Solution
Real world solutions of Non-Semi applications range from problem solving in oil field environments to testing network infrastructure equipment from major telecom manufacturers. Here is a look at one.

Customer: Major manufacturer of industrial electronics
Application: Production test of pressure sensor systems for oil pipeline use.
Need: Each pressure system requires two separately controlled temperature environments. Also, specific throughput requirements.
Temp range: -100°C to +300°C

The Solution



- Center zone and each outer zone are independently controlled
- 4 DUTs are mounted in apertures between the center and an outer zone
- One side of DUT is stressed at hot temperatures while other side at cold
- Simulates real-world stress this DUT sees in the field

VALUATION

Looking at several metrics the stock is undervalued. According to the enterprise multiple, the P/S, and P/E INTT appears undervalued compared to industry.

Metric	inTEST	Industry Average
EV/EBITDA	3.68	8.90

Metric	inTEST	Industry Average
P/E TTM	6.60	14.07
P/E 2012 (E)	10.64	11.85
P/E 2013 (E)	4.85	13-15
P/S	0.75	1.08

Two Stage Free Cash Flow to Equity Model

FCFE = Net Income - Net Capital Expenditure - Change in Net Working Capital + New Debt - Debt Repayment

Assumptions

- The firm is expected to grow at a higher growth rate in the first period.
- The growth rate will drop at the end of the first period to the stable growth rate.

Rationale for using the Model

As the non-semiconductor business ramps up to 50% of total revenues we expect the firm to grow at a higher overall rate than the industry. As These products mature and the firm faces more competition we expect the growth rate to level off.

Weakness of the Model

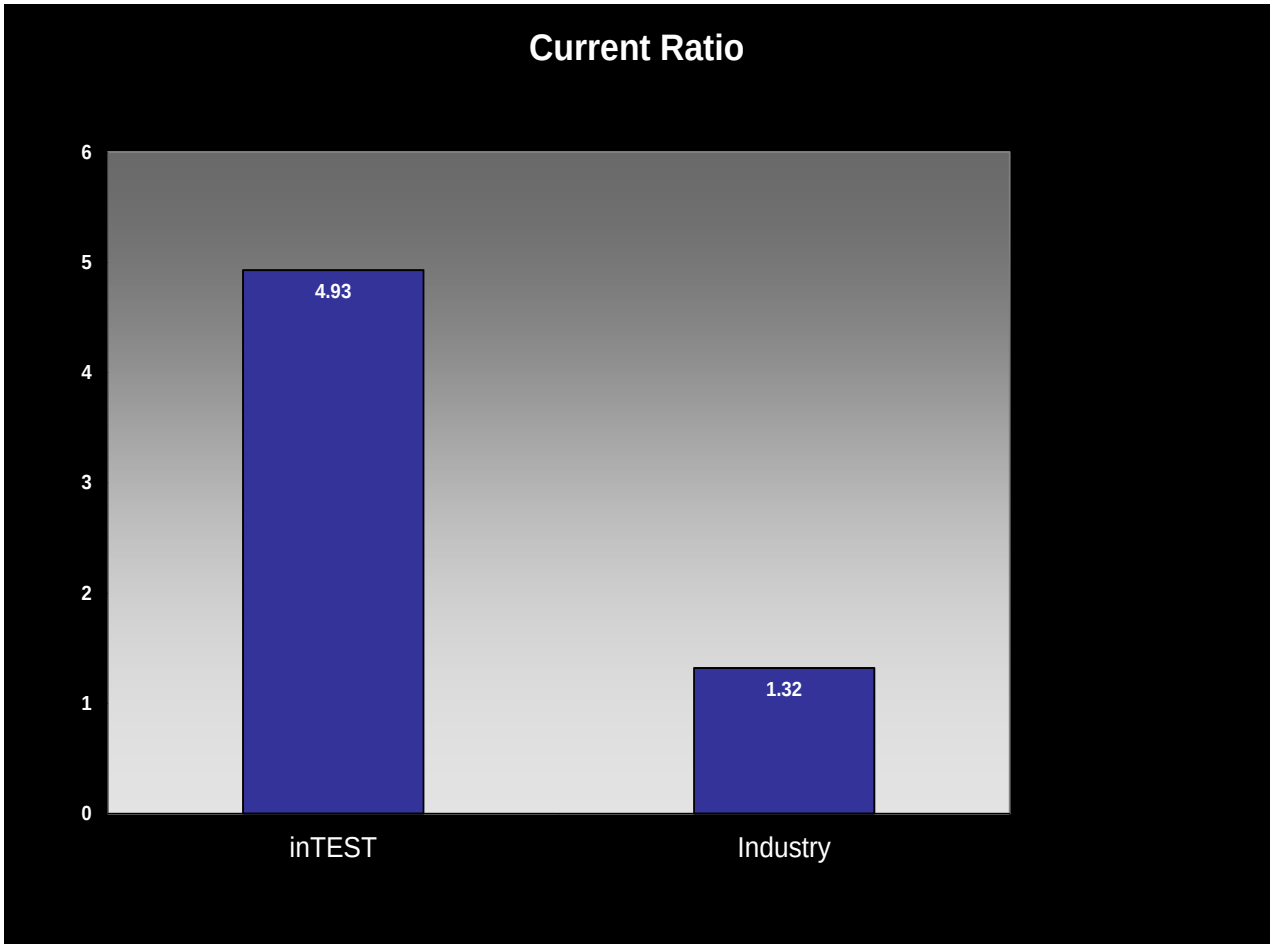
As you add more layers to the model it is more sensitive to the assumptions you make. The growth may look more "lumpy" than we have it in the model.

Output

We used the following inputs:

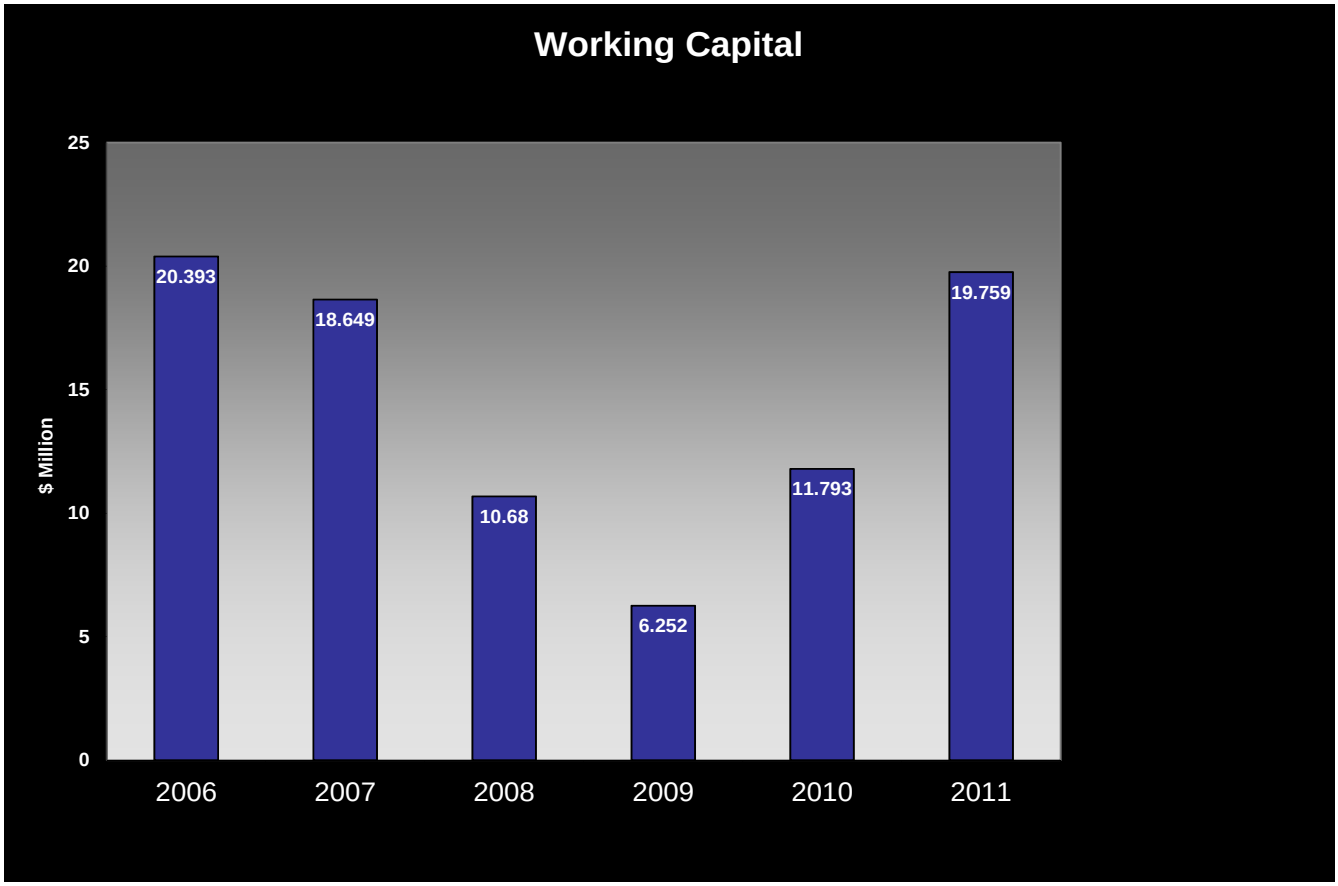
- A 5-year period with an earnings growth rate of 8.0% and a discount rate of 13.77%.
- A continuing period assumed to go on forever, with earnings growing at 5% and a discount rate of 13.05%.

With these inputs we arrive at a target price of $7.23. Our price target of $7.00 per share is the average of 9.9x our 2013 EPS estimate and our two stage model. We would add shares at these levels.



Balance Sheet Analysis

The current ratio can give a sense of the efficiency of a company's operating cycle or its ability to turn its product into cash. Companies that have trouble getting paid on their receivables or have long inventory turnover can run into liquidity problems because they are unable to alleviate their obligations.
Because business operations differ in each industry, it is always more useful to compare companies within the same industry. inTEST current ratio is above the industry average and the firm has been building working capital since 2009.


Working Capital
$ Million
25
20
15
10
5
0
20.393
18.649
10.68
6.252
11.793
19.759
2006
2007
2008
2009
2010
2011

PROJECTED INCOME STATEMENT

INCOME STATEMENT ($ Millions)	Jun-11 Q2 11	Sep-11 Q3 11	Dec-11 Q4 11	Mar-12 Q1 12	Jun-12 Q2 12	Sep-12 Q3 12 E	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012 E	FY 2013 E
REVENUE												
Net Revenue	**13.80**	**11.68**	**10.08**	**10.73**	**13.58**	**10.00**	**38.8**	**23.5**	**46.2**	**47.3**	**46.3**	**56.0**
Sequential Growth		*-15%*	*-14%*	*6%*	*27%*	*-26%*						
OPERATING EXPENSES												
Cost of Revenues	7.00	5.55	5.21	6.14	7.38	5.65	25.0	15.7	24.1	24.4	26.0	28.8
% of Revenue	*50.7%*	*47.5%*	*51.7%*	*57.2%*	*54.4%*	*56.5%*	*64.4%*	*66.8%*	*52.1%*	*51.6%*	*56.2%*	*51.3%*
Gross Profit -	**6.8**	**6.1**	**4.9**	**4.6**	**6.2**	**4.4**	**13.8**	**7.8**	**22.1**	**22.9**	**20.3**	**27.3**
Proforma Gross Margin	*49.3%*	*52.5%*	*48.3%*	*42.8%*	*45.6%*	*43.5%*	*35.6%*	*33.2%*	*47.9%*	*48.4%*	*43.8%*	*48.7%*
R&D + Engg	0.82	0.81	0.80	0.92	0.98	0.88	5.1	2.4	3.0	3.2	3.7	3.9
% of Revenue	*6.0%*	*6.9%*	*7.9%*	*8.6%*	*7.2%*	*8.8%*	*13.0%*	*10.3%*	*6.6%*	*6.9%*	*8.0%*	*7.0%*
SG&A	3.25	2.91	2.89	3.40	3.22	3.15	15.9	9.8	11.8	12	13.02	14.00
% of Revenue	*23.6%*	*24.9%*	*28.7%*	*31.7%*	*23.7%*	*31.5%*	*41.1%*	*41.6%*	*25.4%*	*25.5%*	*28.1%*	*25.0%*
GW Amort, Restructuring, other				*0.36*	-	-	-	-	-		*0.360*	
% of Revenue												
Total Operating Expenses	4.08	3.72	3.69	4.68	4.20	4.03	21.0	12.2	14.8	15	17	18
% of Revenue	*29.5%*	*31.8%*	*36.6%*	*43.6%*	*30.9%*	*40.3%*	*54.1%*	*51.9%*	*32.0%*	*32%*	*37%*	*32%*
Operating Income -	**2.72**	**2.42**	**1.18**	**-0.08**	**1.99**	**0.32**	**-7.2**	**-4.4**	**7.4**	**7.6**	**3.24**	**9.4**
Operating Margin	*19.7%*	*20.7%*	*11.7%*	*-0.8%*	*14.7%*	*3.2%*	*-19%*	*-19%*	*16%*	*16%*	*7%*	*17%*
NON-OPERATING ITEMS												
Non operating Income/Expense	0.01	0.01	0.01	0.01	0.00	0.00	-1.9	-0.5	0.1	0	0.0	0.0
% of Revenue	*0.07%*	*0.04%*	*0.10%*	*0.12%*	*0.00%*	*0.00%*	*-4.80%*	*-2.17%*	*0.11%*	*0.17%*	*0.04%*	*0.00%*
Tax Provision	0.1	-2.8	0.4	0.0	0.7	0.1	0.270	-0.050	0.148	-2.204	0.8	2.3
Effective Tax Rate												
Net Income -	**2.66**	**5.18**	**0.77**	**-0.04**	**1.33**	**0.24**	**-9.33**	**-4.83**	**7.25**	**9.9**	**2.4**	**7.0**
Net Income Margin	*19.2%*	*44.4%*	*7.6%*	*-0.4%*	*9.8%*	*2.4%*	*-24.1%*	*-20.6%*	*15.7%*	*21%*	*5%*	*13%*
Adjustments (for one-time NR items)		**0.28**		**0.07**	**0.00**	**0.00**				**0.29**	**0.07**	**0.00**
EARNINGS PER SHARE												
EPS - Basic	$0.26	$0.22	$0.08	$0.07	$0.13	$0.02	$0.15	-$0.42	$0.72	$0.70	$0.31	$0.69
EPS - Diluted	$0.26	$0.22	$0.08	$0.07	$0.13	$0.02	$0.14	-$0.42	$0.72	$0.69	$0.31	$0.68

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HISTORICAL ZACKS RECOMMENDATIONS



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