

PEAK INTERNATIONAL LTD  
Form 10-Q  
November 09, 2006

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

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**FORM 10-Q**

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(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the Quarterly Period Ended September 30, 2006

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number 0-29332

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**PEAK INTERNATIONAL LIMITED**

(Exact Name of Registrant as Specified in its Charter)

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**Incorporated in Bermuda with limited liability**  
(State or other jurisdiction of

**None**  
(I.R.S. Employer

incorporation or organization)  
Flat E & F, 19/F., CDW Building, 388 Castle Peak Road, Tsuen Wan, New Territories, Hong Kong

Identification Number)

(Address of principal executive offices)

(Zip Code)

(852) 3193-6000

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**Registrant's telephone number, including area code**

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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 twelve months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes  No

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

Large Accelerated Filer  Accelerated Filer  Non-Accelerated Filer

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

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

As of November 7, 2006, Peak International Limited had 12,420,389 shares of common stock outstanding.

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## PART I

## FINANCIAL INFORMATION

Item 1. *Financial Statements*

## Condensed Consolidated Statements of Operations

(in thousands of United States Dollars, except share and per share data)

	Three Months Ended September 30,			
	2006		2005	
	(Unaudited)		(Unaudited)	
Net Sales	\$ 15,817	100.0%	\$ 16,598	100.0%
Cost of Goods Sold	13,193	83.4%	13,610	82.0%
Gross Profit	2,624	16.6%	2,988	18.0%
Selling and Marketing (Note 4)	2,181	13.8%	2,521	15.2%
General and Administrative (Note 4)	1,715	10.8%	1,638	9.9%
Research and Development	28	0.2%	31	0.2%
Loss from operations	(1,300)	(8.2)%	(1,202)	(7.3)%
Other expenses net	(111)	(0.7)%	(157)	(0.9)%
Interest income, net	165	1.0%	112	0.7%
Loss before income taxes	(1,246)	(7.9)%	(1,247)	(7.5)%
Income tax benefit	103	0.7%	91	0.5%
Net Loss	\$ (1,143)	(7.2)%	\$ (1,156)	(7.0)%
LOSS PER SHARE (Note 5)				
Basic	\$ (0.09)		\$ (0.09)	
Diluted	\$ (0.09)		\$ (0.09)	
Weighted Average Number of Shares Outstanding				
Basic	12,420,000		12,420,000	
Diluted	12,420,000		12,420,000	

(See accompanying notes to Unaudited Condensed Consolidated Financial Statements)

**Condensed Consolidated Statements of Operations**

(in thousands of United States Dollars, except share and per share data)

	Six Months Ended September 30,			
	2006 (Unaudited)		2005 (Unaudited)	
Net Sales	\$ 34,470	100.0%	\$ 32,041	100.0%
Cost of Goods Sold	27,011	78.4%	29,689	92.7%
<b>Gross Profit</b>	<b>7,459</b>	<b>21.6%</b>	<b>2,352</b>	<b>7.3%</b>
Selling and Marketing (Note 4)	4,442	12.9%	5,296	16.5%
General and Administrative (Note 4)	3,295	9.6%	3,397	10.6%
Research and Development	64	0.2%	75	0.2%
Gain on Disposal of a Subsidiary (Note 11)			(2,189)	(6.8)%
<b>Loss from operations</b>	<b>(342)</b>	<b>(1.0)%</b>	<b>(4,227)</b>	<b>(13.2)%</b>
Other expenses net	(166)	(0.5)%	(291)	(0.9)%
Interest income, net	282	0.8%	217	0.6%
<b>Loss before income taxes</b>	<b>(226)</b>	<b>(0.7)%</b>	<b>(4,301)</b>	<b>(13.5)%</b>
Income tax benefit	21	0.1%	533	1.7%
<b>Net Loss</b>	<b>\$ (205)</b>	<b>(0.6)%</b>	<b>\$ (3,768)</b>	<b>(11.8)%</b>
<b>LOSS PER SHARE (Note 5)</b>				
Basic	\$ (0.02)		\$ (0.30)	
Diluted	\$ (0.02)		\$ (0.30)	
<b>Weighted Average Number of Shares Outstanding</b>				
Basic	12,420,000		12,420,000	
Diluted	12,420,000		12,420,000	

(See accompanying notes to Unaudited Condensed Consolidated Financial Statements)

## Condensed Consolidated Balance Sheets

(in thousands of United States Dollars, except share and per share data)

	September 30,	March 31,
	2006 (Unaudited)	2006 (Audited)
<b>ASSETS</b>		
Current Assets:		
Cash and cash equivalents	\$ 19,548	\$ 17,441
Restricted cash (Note 12)	1,128	2,182
Accounts receivable net of allowance for doubtful accounts of \$236 at September 30, 2006 and \$128 at March 31, 2006	12,007	12,277
Inventories (Note 2)	13,595	12,782
Other receivables, deposits and prepayments	855	615
Total Current Assets	47,133	45,297
Property, Plant and Equipment net	21,601	22,358
Land Use Right	717	722
Deposits for Acquisition of Property, Plant and Equipment	279	133
Other deposit (Note 3)	301	301
<b>TOTAL ASSETS</b>	<b>\$ 70,031</b>	<b>\$ 68,811</b>
<b>LIABILITIES AND SHAREHOLDERS EQUITY</b>		
Current Liabilities:		
Accounts payable:		
-trade	\$ 6,603	\$ 5,601
-property, plant and equipment	513	536
Accrued payroll and employee benefits	1,323	1,007
Accrued other expenses	1,689	2,019
Income taxes payable	114	111
Total Current Liabilities	10,242	9,274
Deferred Income Taxes	263	288
Total Liabilities	10,505	9,562
Commitments and Contingencies (Note 9)		
Shareholders' Equity:		
Common stock, \$0.01 par value; authorized 100,000,000 shares; issued and outstanding 12,420,389 shares at September 30, 2006 and at March 31, 2006	124	124
Additional paid-in capital	27,517	27,135
Retained earnings	33,033	33,238
Accumulated other comprehensive loss	(1,148)	(1,248)
Total shareholders' equity	59,526	59,249
<b>TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY</b>	<b>\$ 70,031</b>	<b>\$ 68,811</b>

(See accompanying notes to Unaudited Condensed Consolidated Financial Statements)



**Condensed Consolidated Statements of Cash Flows**

(in thousands of United States Dollars)

	Six Months Ended September 30,	
	2006	2005
	(Unaudited)	(Unaudited)
<b>Operating activities:</b>		
Net loss	\$ (205)	\$ (3,768)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities:		
Depreciation and amortization	3,365	3,208
Deferred income taxes	(25)	(588)
Loss on disposal/write-off of property, plant and equipment	74	331
Allowance for doubtful accounts	108	14
Non-cash share-based compensation	382	
Gain on disposal of a subsidiary		(2,189)
Changes in operating assets and liabilities:		
Accounts receivable	162	(929)
Inventories	(813)	2,819
Other receivables, deposits and prepayments	(240)	(225)
Income taxes receivable		3
Accounts payable trade	1,002	(3,804)
Accrued payroll, employee benefits and other expenses	(14)	2,072
Income taxes payable	3	3
Cash held in an escrow for terms of sale agreement for disposal of a subsidiary (Note 11)	641	
Cash held in another escrow for funding of certain contingent obligations under existing contracts with senior management (Note 12)	413	
<b>Net cash provided by (used in) operating activities</b>	<b>4,853</b>	<b>(3,053)</b>
<b>Investing activities:</b>		
Net proceeds on disposal of a subsidiary		2,254
Acquisition of property, plant and equipment	(2,700)	(2,135)
(Increase) decrease in deposits for acquisition of property, plant and equipment	(146)	33
<b>Net cash (used in) provided by investing activities</b>	<b>(2,846)</b>	<b>152</b>
<b>Net increase (decrease) in cash and cash equivalents</b>	<b>2,007</b>	<b>(2,901)</b>
Cash and cash equivalents at beginning of period	17,441	22,301
Effects of exchange rate changes on cash and cash equivalents	100	3
<b>Cash and cash equivalents at end of period</b>	<b>\$ 19,548</b>	<b>\$ 19,403</b>
<b>Supplemental cash flow information:</b>		
Cash paid during the period		
Income taxes	1	49

(See accompanying notes to Unaudited Condensed Consolidated Financial Statements)

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**Notes to Condensed Consolidated Financial Statements**

**(in thousands of United States Dollars, except share and per share data, unaudited)**

**(1) Organization and basis of presentation**

Peak International Limited (the Company) was incorporated as an exempted company with limited liability in Bermuda under the Companies Act 1981 of Bermuda (as amended) on January 3, 1997. The subsidiaries of the Company are principally engaged in the manufacture and sale of precision-engineered packaging products, such as matrix and disk drive trays, reels and carrier tapes used in the storage and transportation of semiconductor devices and other electronic components. The Company's principal production facilities are located in the People's Republic of China (the PRC). The Company maintains sales offices in Hong Kong, the PRC, Malaysia, Singapore, Taiwan, and the United States, whereby direct sales are made to customers, and representative offices in the PRC, the Philippines, and Italy, that provide customers with technical information. The Company also sells its products through a sales agent located in South Korea.

The unaudited condensed consolidated financial statements include the accounts of the Company and its subsidiaries. All significant intra-group balances and transactions have been eliminated on consolidation.

The accompanying condensed consolidated financial information has been prepared by the Company without being audited, in accordance with the instructions to Form 10-Q and therefore does not include all information and footnotes necessary for a fair presentation of financial position, results of operations and cash flows in accordance with accounting principles generally accepted in the United States of America, consistent in all material respects with those applied in the Company's Annual Report on Form 10-K for the fiscal year ended March 31, 2006, except for the April 1, 2006 adoption of Statement of Financial Accounting Standards No. 123R, *Share-Based Payment* (SFAS 123R). See Note 4.

The preparation of financial statements in conformity with generally accepted accounting principles requires the use of estimates and assumptions that affect reported amounts of certain assets, liabilities, revenues and expenses as of and for the reporting periods. Actual results could differ from those estimates. Differences from those estimates are reported in the period they become known.

The unaudited condensed consolidated financial statements reflect all adjustments (including normal recurring adjustments) which in the opinion of management are required for a fair presentation of the Company's interim results. The results for interim periods are not necessarily indicative of the results that may be achieved in the entire year. These condensed consolidated financial statements and notes thereto should be read together with the consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the year ended March 31, 2006.

**New Accounting Standards**

In June 2006, the Financial Accounting Standards Board (FASB) ratified the provisions of Emerging Issues Task Force (EITF) Issue No. 06-3, *How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross versus Net Presentation)*. EITF Issue No. 06-3 requires that the presentation of taxes within revenue-producing transactions between a seller and a customer, including but not limited to sales, use, value added, and some excise taxes, should be on either a gross (included in revenue and cost) or a net (excluded from revenue) basis. In addition, for any such taxes that are reported on a gross basis, a company should disclose the amounts of those taxes in interim and annual financial statements for each period for which an income statement is presented if those amounts are significant. The disclosure of those taxes can be done on an aggregate basis. EITF Issue No. 06-3 is effective for fiscal years beginning after December 15, 2006, which will be our fiscal 2008. The adoption of EITF Issue No. 06-3 is not expected to have a material impact on our consolidated results of operations or financial position.

In June 2006, the FASB issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*—an interpretation of FASB Statement No. 109 (FIN 48) which prescribes a recognition threshold and measurement attribute, as well as criteria for subsequently recognizing, derecognizing and measuring uncertain tax positions for financial statement purposes. FIN 48 also requires expanded disclosure with respect to the uncertainty in income tax assets and liabilities. FIN 48 is effective for fiscal years beginning after December 15, 2006, which will be our fiscal 2008, and is required to be recognized as a change in accounting principle through a cumulative-effect adjustment to retained earnings as of the beginning of the year of adoption. The adoption of FIN 48 is not expected to have a material impact on our consolidated results of operations or financial position.



## Notes to Condensed Consolidated Financial Statements (continued)

(in thousands of United States Dollars, except share and per share data, unaudited)

**(2) Inventories**

The components of inventories were as follows:

	September 30,	March 31,
	2006	2006
	(Unaudited)	
Raw materials	\$ 6,116	\$ 5,152
Finished goods	7,479	7,630
	\$ 13,595	\$ 12,782

**(3) Other Deposit**

This represents the security bond placed at a Taiwanese court in order to obtain an anti-injunction order in respect of a potential patent dispute in Taiwan. See Note 9(a) *Litigation*. Management of the Company does not expect the case to be settled within 12 months and therefore the amount was classified as a non-current asset as at September 30, 2006.

**(4) Non-cash Share-based Compensation**

Prior to April 1, 2006, the Company accounted for share-based employee compensation, including stock options, using the method prescribed in Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* and related Interpretations ( APB 25 ). Under APB 25, stock options are granted at market price and no compensation cost is recognized, and a disclosure is made regarding the pro forma effect on net earnings assuming compensation cost had been recognized in accordance with Statement of Financial Accounting Standards No. 123, *Accounting for Stock-Based Compensation* ( SFAS 123 ). In December 2004, the Financial Accounting Standards Board ( FASB ) issued SFAS 123R, which requires companies to measure and recognize compensation expense for all share-based payments at fair value. SFAS 123R eliminates the ability to account for share-based compensation transactions using APB 25, and generally requires that such transactions be accounted for using prescribed fair-value-based methods. SFAS 123R permits public companies to adopt its requirements using one of two methods: (a) a modified prospective method in which compensation costs are recognized beginning with the effective date based on the requirements of SFAS 123R for all share-based payments granted or modified after the effective date, and based on the requirements of SFAS 123 for all awards granted to employees prior to the effective date of SFAS 123R that remain unvested on the effective date or (b) a modified retrospective method which includes the requirements of the modified prospective method described above, but also permits companies to restate based on the amounts previously recognized under SFAS 123 for purposes of pro forma disclosures either for all periods presented or prior interim periods of the year of adoption. Effective April 1, 2006, the Company adopted SFAS 123R using the modified prospective method. No share-based employee compensation cost has been reflected in net income prior to the adoption of SFAS 123R. Results for prior periods have not been restated.

## Notes to Condensed Consolidated Financial Statements (continued)

(in thousands of United States Dollars, except share and per share data, unaudited)

The following table presents the share-based compensation expense recognized in accordance with SFAS 123R during the quarter and the six months ended September 30, 2006, and a pro forma disclosure in accordance with APB 25 during the quarter and the six months ended September 30, 2005 which amounts were accordingly not recognized in the accompanying financial statements:

	Three Months Ended September 30,		Six Months Ended September 30,	
	2006	2005	2006	2005
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
The components of non-cash share-based compensation were as follows:				
Selling and Marketing	\$ 51	(83)	\$ 121	(35)
General and Administrative	166	(279)	261	(194)
	\$ 217	\$ (362)	\$ 382	\$ (229)

The adoption of SFAS 123R reduced income before income tax expense and net income for the quarter and for the six months ended September 30, 2006 by \$0.2 million and \$0.4 million, respectively. Basic and diluted loss per share for the quarter ended September 30, 2006 would have been \$0.07 while basic and diluted earnings per share of \$0.01 would have been recorded for the six months ended September 30, 2006 if the Company had not adopted SFAS 123R, compared to reported basic and diluted losses per share of \$0.09 and \$0.02 respectively for the quarter and for the six months ended September 30, 2006. The total value of the stock options awards is expensed ratably over the service period of the employees receiving the awards. As of September 30, 2006, total unrecognized compensation cost related to stock-based options and awards was \$1.3 million and the related weighted-average period over which it is expected to be recognized is approximately 2 years.

**Stock Option Plans**

At September 30, 2006, the Company had two active share-based employee compensation plans, the 1997 Stock Option Plan and the 1998 Stock Option Plan. Stock option awards granted from these plans are granted at the fair market value on the date of grant, and vest over a period determined at the time the options are granted, generally ranging from zero to three years, and generally have a maximum term of ten years. During the quarter and the six months ended September 30, 2006, the Company issued options for 250,000 and 455,000 shares under the 1998 Stock Option Plan at weighted-average exercise prices of \$3.05 and \$3.07 per share to directors and employees of the Company, respectively. The Company did not issue any shares under the 1997 Stock Option Plan during the quarter and the six months ended September 30, 2006.

For all stock options, the Company recognizes compensation cost on a straight-line basis over the requisite service period. When the options are exercised, the Company issues common stock from its treasury shares.

## Notes to Condensed Consolidated Financial Statements (continued)

(in thousands of United States Dollars, except share and per share data, unaudited)

The following is a summary of stock option activity within the Company's share-based compensation plans and charges for the quarter and the six months ended September 30, 2006:

	Number of Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (In Thousands)
Options outstanding:				
Balance at April 1, 2006	2,200,057	\$ 5.12		
Granted	455,000	\$ 3.07		
Exercised				
Forfeited	(235,442)	6.16		
Outstanding at September 30, 2006	2,419,615	4.64	2.69	\$ 27
Exercisable at September 30, 2006	1,723,180	\$ 5.20	2.39	\$ 8

The aggregate intrinsic value in the table above represents the total pre-tax intrinsic value (the difference between the Company's closing stock price on the last trading day of the second quarter of fiscal 2007 and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders had all option holders exercised their options on September 30, 2006. This amount changes based on the fair market value of the Company's stock.

No options were exercised during the quarter and the six months ended September 30, 2006.

The weighted average fair value of stock option awards granted and the key assumptions used in the Black-Scholes valuation model to calculate the fair value are as follows:

	Three Months Ended September 30,		Six Months Ended September 30,	
	2006	2005	2006	2005
Weighted average fair value of options granted	\$ 1.28	\$ 1.24	\$ 1.32	\$ 1.45
Key assumptions used in determining the fair value:				
Weighted average risk free interest rate	5.01%	4.08%	5.02%	3.78%
Expected life of the option (in years)	3.00	3.00	3.00	3.00
Expected volatility of underlying stocks	57.0%	56.1%	58.1%	60.3%
Expected dividend yield				

\* The risk-free interest rate is based on the U.S. Treasury zero-coupon yield with a maturity that approximates the expected life of options.

\*\* The expected life of options is based on historical data of the Company.

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\*\*\* The expected volatility of underlying stocks is measured using historical daily price changes of the Company's common stock over the expected life of options.

## Notes to Condensed Consolidated Financial Statements (continued)

(in thousands of United States Dollars, except share and per share data, unaudited)

The Black-Scholes option valuation model was developed for use in estimating the fair value of traded options which have no vesting restrictions and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions, including the expected volatility of underlying stocks. Because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

The following table illustrates the effect on net loss and net loss per share for the three and six months ended September 30, 2005 as if the Company had applied the fair value recognition provisions of SFAS 123R to all outstanding stock option awards for periods presented prior to the Company's adoption of SFAS 123R:

	Three Months Ended September 30, 2005	Six Months Ended September 30, 2005
Net loss, as reported	\$ (1,156)	\$ (3,768)
Deduct total stock-based compensation expense released under a fair value method for all awards	362	229
Pro forma net loss	\$ (794)	\$ (3,539)
Net loss per share:		
Basic and diluted, pro forma	\$ (0.06)	\$ (0.28)
Basic and diluted weighted average shares used in pro forma computation :	12,420,388	12,420,388

**(5) Loss Per Share**

The following is a reconciliation of the numerator and the denominator of the basic losses per share:

	Three Months Ended September 30, 2006 (unaudited)	September 30, 2005 (unaudited)	Six Months Ended September 30, 2006 (unaudited)	September 30, 2005 (unaudited)
<b>Numerator:</b>				
Net loss	\$ (1,143)	\$ (1,156)	\$ (205)	\$ (3,768)
<b>Denominator:</b>				
Weighted average number of shares outstanding				
Basic	12,420,389	12,420,388	12,420,389	12,420,388
Assumed exercise of stock options				
Diluted	12,420,389	12,420,388	12,420,389	12,420,388

For the quarter and for the six months ended September 30, 2006 and September 30, 2005, exercise of all outstanding stock options would have been anti-dilutive and such stock options were therefore not included in the computation of diluted loss per share.

## Notes to Condensed Consolidated Financial Statements (continued)

(in thousands of United States Dollars, except share and per share data, unaudited)

**(6) Comprehensive Loss**

Comprehensive loss is defined as the aggregate change in shareholders' equity excluding changes in ownership interests. The components of comprehensive loss are as follows:

	Three Months Ended September 30,		Six Months Ended September 30,	
	2006	2005	2006	2005
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
Net loss	\$ (1,143)	\$ (1,156)	\$ (205)	\$ (3,768)
Other comprehensive income:				
Foreign currency translation	7	85	100	3
Comprehensive loss	\$ (1,136)	\$ (1,071)	(105)	(3,765)

**(7) Employee Stock Purchase Plan**

Under SFAS 123R, the Company's Employee Stock Purchase Plan is considered compensatory. During the quarter and the six months ended September 30, 2006, the Company did not issue any shares under the 2000 Employee Stock Purchase Plan.

**(8) Share Repurchase**

In September 2000, the Board of Directors authorized the repurchase, at management's discretion, of up to \$10,000 of the Company's common stock at prices not to exceed 150% of the Company's net asset value per share. Common stock repurchased will be cancelled immediately. The excess of purchase price over par value is charged to additional paid-in capital.

There was no repurchase of shares for the quarter and for the six months ended September 30, 2006 and 2005.

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Notes to Condensed Consolidated Financial Statements (continued)

(in thousands of United States Dollars, except share and per share data, unaudited)

**(9) Commitments and Contingencies**

**(a) Litigation**

R.H. Murphy Co., Inc. ( Murphy ) is the owner of U.S. Re-examined Patent 5,400,904 C1 and certain corresponding foreign patents, which are directed to specific features in trays used to carry integrated circuits. Murphy has notified us and certain of our customers that it believes these patents are infringed by certain integrated circuit trays that we provided to our customers, and indicated that licenses to these patents are available. We do not believe that any valid claim of these patents is infringed, and are proceeding consistent with that belief.

We applied for a preliminary injunction order so that we can continue to sell trays in Taiwan without being interrupted by Murphy and its three distributors in Taiwan and the Taiwan Taichung District Court granted the preliminary injunction order in June 2002. On July 8, 2002, we placed a security bond of approximately \$301 at the Taiwan Taichung District Court for a compulsory execution of the preliminary injunction order. Murphy and its three local distributors filed an appeal with the Taiwan High Court, Taichung Branch against the grant of the order by the district court, and in December 2002, the High Court revoked the order issued by the district court. In January 2003, we filed a re-appeal with the Taiwanese Supreme Court, and the Supreme Court revoked the High Court's ruling and dismissed Murphy and its local distributors' appeal filed with the High Court. The grant of the preliminary injunction order has now become final and, accordingly, it is unlikely that Murphy or its local distributors will be able to obtain preliminary injunctive relief against us or our Taiwan customers during the pendency of the underlying litigation. In addition, in October 2002, we filed a civil suit against Murphy with the Taiwan Taichung District Court seeking permanent relief in connection with the preliminary injunction order, which is pending before the Taiwan High Court, Taichung Branch. An additional security bond of approximately \$13 was placed with the Taiwan Taichung District Court in connection with the underlying civil suit, which was later increased by approximately \$24. If our effort to receive permanent relief is not successful, we may be required to forfeit the bonds and Murphy and its distributors in Taiwan may assert patent infringement claims against us, which, if successful, could prevent us from selling certain of our products in Taiwan and could result in monetary damages. In December 2001 and July 2003, we also filed two cancellation actions with the Taiwanese Intellectual Property Office ( IPO ) to invalidate Murphy's patent. The IPO rejected the cancellation actions, and we filed an administrative appeal and further filed an administrative suit for each of the cases, which are pending before the Taiwan High Administrative Court. In February 2002, we also filed a complaint for unfair competition with the Fair Trade Commission ( FTC ) against Murphy. The FTC dismissed the action and we have filed an administrative appeal. That appeal was dismissed and we filed an administrative suit. The Taipei High Administrative Court rendered a judgment favorable to Peak, ruling that Murphy violated the Fair Trade Act. Murphy then filed an appeal, which is still pending before the Supreme Administrative Court. At present, the outcome of this patent dispute cannot be predicted with reasonable particularity and no impact to the financial statements has been reflected in this respect.

**(b) Commitments**

At September 30, 2006, the Company had commitments for capital expenditures of approximately \$189.

## Notes to Condensed Consolidated Financial Statements (continued)

(in thousands of United States Dollars, except share and per share data, unaudited)

## (10) Segment Information

	Hong Kong & the PRC	United States	Other Asian countries	Eliminations	Consolidated
<b>Three months ended September 30, 2006 and 2005</b>					
Quarter ended September 30, 2006					
Net sales to third parties	\$ 8,255	\$ 756	\$ 6,806	\$	\$ 15,817
Transfer between geographic areas	7,298		1,458	(8,756)	
Total net sales	\$ 15,553	\$ 756	\$ 8,264	\$ (8,756)	\$ 15,817
(Loss) Income before tax	\$ (1,530)	\$ 227	\$ (3)	\$ 60	\$ (1,246)
Quarter ended September 30, 2005					
Net sales to third parties	\$ 8,666	\$ 1,291	\$ 6,641	\$	\$ 16,598
Transfer between geographic areas	7,683		853	(8,536)	
Total net sales	\$ 16,349	\$ 1,291	\$ 7,494	\$ (8,536)	\$ 16,598
(Loss) Income before tax	\$ (1,210)	\$ 100	\$ (250)	\$ 113	\$ (1,247)
<b>Six months ended September 30, 2006 and 2005</b>					
Six months ended September 30, 2006					
Net sales to third parties	\$ 17,375	\$ 3,264	\$ 13,831	\$	\$ 34,470
Transfer between geographic areas	15,695		2,866	(18,561)	
Total net sales	\$ 33,070	\$ 3,264	\$ 16,697	\$ (18,561)	\$ 34,470
(Loss) Income before tax	\$ (828)	\$ 437	\$ 205	\$ (40)	\$ (226)
Six months ended September 30, 2005					
Net sales to third parties	\$ 16,253	\$ 2,315	\$ 13,473	\$	\$ 32,041
Transfer between geographic areas	14,810		1,952	(16,762)	
Total net sales	\$ 31,063	\$ 2,315	\$ 15,425	\$ (16,762)	\$ 32,041
(Loss) Income before tax	\$ (4,374)	\$ 209	\$ (414)	\$ 278	\$ (4,301)

## (11) Gain on Disposal of a Subsidiary

A former subsidiary of the Company ( Warden ) owned certain land use rights and an incomplete industrial building in Shenzhen, the PRC. The incomplete industrial building was originally purchased with the intention of completing the facility for expansion of our existing production facilities but this plan was subsequently aborted. During the fourth quarter of the year ended March 31, 2001, management reassessed the fair value of the building given the downturn in the industrial property market in which the building was located and a provision of \$759 was recorded to reduce the carrying value of the building.



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During the quarter ended June 30, 2002, the incomplete industrial building and the related land use rights in the PRC, which had an assigned period for 50 years commencing May 1993, were reclassified as asset to be disposed of by sale following management's decision to dispose of the property as a general purpose industrial building. As a result, the property was written down to its fair market value less costs to sell pursuant to SFAS No. 144 Accounting for the Impairment of Disposal of Long-Lived Assets, resulting in an asset impairment charge of \$13,378 during the year ended March 31, 2003. The net book value of the property and the land use rights were \$4,071 and \$1,159, respectively, as of March 31, 2005 and 2004.

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**Notes to Condensed Consolidated Financial Statements (continued)**

**(in thousands of United States Dollars, except share and per share data, unaudited)**

The Company entered into a contract with an independent third party (the Purchaser) for the sale of Warden. The sale was completed on April 13, 2005 for approximately \$7,692 in cash. Approximately \$1,282 of the sale proceeds was initially held in escrow as restricted cash (see Note 12, Restricted Cash). A net gain on disposal of approximately \$2,189 was recognized in the second quarter of fiscal 2006.

The escrow fund extends over two consecutive years, commencing with the completion of the sale on April 13, 2005, as follows:

The year ended April 13, 2006; and

The year ending April 13, 2007.

In accordance with the terms of the sale agreement, immediately following the year ended April 13, 2006, approximately \$641, which represented one half of the full amount established and held in escrow and classified as restricted cash, was released to the Company without any reduction or offsets.

During the year ending April 13, 2007, the remaining escrow fund shall be distributed in the following order:

First, towards payment of any tax or duty payable in respect of the remaining escrow fund for which the Company or the escrow agent is or are or may be properly become liable and towards payment of any bank or other charges during the year; and

Secondly, by payment to the Purchaser of any amount of the remaining escrow fund in or towards satisfaction of such amount payable by the Company as stated in any final judgment or award made or ordered during the year in respect of any litigation, arbitration or other legal proceedings the subject matter of a claim, and if applicable, by payment to the Purchaser of an amount equivalent to the interest that would have been earned on such amount during the year.

On or immediately after April 13, 2007, the remaining escrow fund shall be closed and be distributed:

First, by payment to the Purchaser of such amount, if any, which has been agreed to by the Company in compensation for any claim, and an amount equivalent to the interest that would have been earned on such amount since the completion of the sale on April 13, 2005; and

Secondly, by payment of the balance to the Company.

The Company is liable to compensate the Purchaser for any breach of warranties that include the Company being the legal and beneficial owner of the shares of Warden, free and clear of encumbrances or third party right, before they were sold to the Purchaser, and that no legal proceedings have been initiated or are outstanding against Warden and there are no unfulfilled or unsatisfied judgment or court orders against Warden. If the Purchaser and the Company shall not have reached agreement as to the amount to which the Purchaser is entitled by way of compensation in respect of any of the aforesaid claims, the matter in dispute will be determined by an independent solicitor of appropriate experience and standing. The sale agreement is governed by and construed in accordance with the laws of Hong Kong and the parties agree to submit to the exclusive jurisdiction of the courts of Hong Kong. Management is not aware of any potential claim or encumbrance in connection with the sale agreement and no such claim or encumbrance has been alleged by the Purchaser or any other party.

**Notes to Condensed Consolidated Financial Statements (continued)**

**(in thousands of United States Dollars, except share and per share data, unaudited)**

**(12) Restricted Cash**

As at September 30, 2006, \$641 of the sale proceeds were held in escrow as restricted cash described in Note 11 above, Gain on Disposal of a Subsidiary.

In addition to this, on October 14, 2005, the Company entered into escrow arrangements appointing an independent third party as an escrow agent ( Escrow Agent ) for a total of \$2,501 deposited as restricted cash by the Company. In September 2005, a shareholder of the Company stated its intention to replace the Company's senior management and effect a merger of the Company with another corporation. The escrows were set up to ensure that obligations of the Company to the officers under their employment contracts would be honored in the future. The Company deposited an amount equal to estimated severance payments and anticipated administrative costs in the escrows. During the fourth quarter of fiscal 2006, severance payments of \$1,600 were paid to the former Chief Executive Officer and the former Vice President, General Counsel. During the six months ended September 30, 2006, severance payments of \$170 were paid to two other former senior executives of the Company and \$243 was released back to the Company as free cash as a result of the resignation of a former senior executive of the Company. The remaining funds of \$487 in these escrows will not be available for use by the Company until March 15, 2007 or earlier in accordance with the provisions of the escrow agreements.

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

The following management's discussion and analysis of financial condition and results of operations is based upon and should be read together with the consolidated financial statements of the Company and notes thereto included in this Report and the Registrant's Annual Report on Form 10-K for the year ended March 31, 2006.

*Forward-Looking Statements*

Management's discussion and analysis of financial condition and results of operations and other sections of this Report contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. We intend for the forward-looking statements to be covered by the safe harbor provisions for forward-looking statements in these sections. These statements, which include statements regarding our beliefs regarding the benefits of our recycling business, our beliefs regarding our distribution capabilities, our beliefs regarding the benefits of our products, our beliefs regarding the benefits of our in-house tooling facilities, our expectation that we will meet our cash requirements for 2007 from cash flows from operations, our plans to expand capacity and replace fixed assets (including the expectation to fund such plans through current cash reserves), our beliefs that we are not contractually obligated to pay taxes and other amounts owed by the factory at which our products are manufactured and our expectations regarding the assessment of any penalties on such amounts, our expected financial position, business and financing plans, our beliefs that our existing cash and cash equivalents and anticipated cash flow from operations will be sufficient to meet our anticipated cash needs in the ordinary course of business for at least the next 12 months, our expectation that we will be able to renegotiate the terms and conditions of our processing agreement, our beliefs that our operations in the PRC are now in compliance with the applicable PRC legal and regulatory requirements relating to environmental matters and custom duties, statements regarding intellectual property rights of third parties, statements regarding our critical accounting policies, statements regarding the validity of lawsuits against us, and statements regarding the expected release of escrow funds to us in connection with a sale of a former subsidiary. Such forward-looking statements are identified by use of forward-looking words such as anticipates, believes, plans, estimates, expects, and intends or words or phrases of similar expression. These forward-looking statements are subject to various assumptions, risks and uncertainties, including but not limited to, economic conditions in the semiconductor and disk drive industries, any future economic downturn, demand for the Company's products, the Company's dependence on significant customers, technology developments affecting the Company's products, the Company's ability to raise additional capital if necessary, the price and availability of raw materials, fluctuations in currency markets, the outcome of lawsuits by and against the Company, difficulties related to working in the PRC, including regional government and processing partner relations and contracts, foreign currency exchange laws, taxation and health issues, and amounts the Company may have to pay for back taxes and social insurance contributions to the PRC tax authorities. Actual results could differ materially from those contemplated by the forward-looking statements as a result of these factors and those set forth under Item 1A of Part II Risk Factors in this Quarterly Report and in our Annual Report on Form 10-K for the fiscal year ended March 31, 2006. These forward-looking statements speak only as of the date hereof. The Company expressly disclaims any obligation or undertaking to release publicly any updates or revisions to any forward-looking statements contained herein to reflect any change in the Company's expectations with regard hereto or any change in events, conditions or circumstances on which any such statement is based. Investors are cautioned not to place undue reliance on these forward-looking statements.

All references to the Company, Peak, we, us or our herein are references to Peak International Limited, a company incorporated under Bermuda law on January 3, 1997, and, unless the context otherwise requires, its subsidiaries and predecessors. All references to Peak (HK) herein are to Peak Plastic & Metal Products (International) Limited, a company incorporated in Hong Kong and a wholly-owned subsidiary of the Company and, unless the context otherwise requires, its subsidiaries and predecessors. References in this Quarterly Report on Form 10-Q (Quarterly Report) to our historical business and operations assume that the corporate reorganization in 1997 (the Restructuring) by which, among other things, Peak (HK) became a wholly-owned subsidiary of the Company and the Company acquired its other subsidiaries, had already occurred as of the times to which the references relate. Any discrepancies in the tables included in this Quarterly Report between the amounts indicated and the totals thereof are due to rounding. All references to US Dollars, US\$ or \$ herein are to United States dollars, references to HK Dollars or HK\$ are to Hong Kong dollars.

*Results of Operations*

*Net Sales.* Net sales decreased by approximately 4.7% to \$15.8 million in the second quarter of fiscal 2007 from \$16.6 million in the same quarter of fiscal 2006. The decrease was primarily due to decrease in sales of disk drive trays and disc caddies. Net sales of semiconductor trays increased slightly by 0.5% over the same quarter last year, reflecting a 1.1% increase in sales volume, and a 0.6% decrease in average selling price. For the second quarter of fiscal 2007, net sales of tapes and reels increased by 6.0% compared to the second quarter of fiscal 2006, primarily due to a 6.5% increase in sales volume combined with a 0.4% decrease in average selling price.

Net sales of disk drive trays decreased by 44.3% compared to the same period last year, reflecting a 46.7% decrease in sales volume and a 4.5% increase in average selling price. Net sales for disc caddies, a relatively new product that was first introduced just over a year ago, decreased due to the rationalization of inventory with the integration of one customer into another of our customer. Our disk drive tray sales and new product sales have generally been to a few major customers or to subcontractors supporting those customers. These sales are largely dependent on the introduction of new products by those customers. New product introductions are difficult to forecast with respect to both timing and demand. As a result, sales of our disk drive trays and new products have, and will in the future, fluctuate dramatically with the corresponding fluctuations in the introduction of new products.

Net sales increased by approximately 7.6% to \$34.5 million for the six months ended September 30, 2006 from \$32.0 million for the six months ended September 30, 2005. Net sales of semiconductor trays increased by 10.4% comparing the six months ended September 30, 2006 to the six months ended September 30, 2005, primarily due to an increase in sales volume by 8.5% and a 1.7% increase in average selling price. Comparing the same six-month periods, net sales of tapes and reels increased by 10.9%, primarily due to a 9.8% increase in sales volume and a 1.0% increase in average selling price, while net sales of disk drive trays reduced by half and net sales of disc caddies tripled.

*Gross Profit.* Gross profit decreased to \$2.6 million in the second quarter of fiscal 2007 from \$3.0 million in the second quarter of fiscal 2006. Gross margin as a percentage of sales dropped to 16.6% in the second quarter of fiscal 2007 from 18.0% in the same quarter of fiscal 2006. The gross margin was unfavorably impacted by several factors. First, the reduced sales resulted in a greater proportion of fixed manufacturing overheads that was absorbed into the cost of goods sold. Second, the gross margin included an exceptional charge of approximately \$0.8 million for materials that were written down to scrap value as they were no longer usable in the production process. Third, there was a loss of approximately \$0.1 million from the conclusion of contract litigation with a scrap dealer.

Gross profit increased to \$7.5 million for the six months ended September 30, 2006 from \$2.4 million for the six months ended September 30, 2005. Gross margin increased as a percentage of sales to 21.6% for the six months ended September 30, 2006 from 7.3% for the six months ended September 30, 2005. The gross profit for the six months ended September 30, 2005 included approximately \$2.0 million of expenses related to income taxes for employees of the Company, its affiliates or other companies who performed services at the factory, severance payments of approximately \$0.4 million to workers at the factory, and write-offs of machinery and molds amounting to approximately \$0.3 million. Also, higher materials usage and labor costs as a result of changes in product mix, cost of raw materials and labor overtime resulted in an adverse impact of approximately \$2.1 million for the six months ended September 30, 2005.

*Loss from Operations.* Operating loss of \$1.3 million was recorded in the second quarter of fiscal 2007 compared to an operating loss of \$1.2 million in the second quarter of fiscal 2006. Operating loss margin was 8.2% for the second quarter of fiscal 2007, in comparison to 7.3% for the second quarter of fiscal 2006. The increase in operating loss was primarily due to the decrease in gross margin, which was partially offset by a reduction in selling and marketing expenses.

Operating loss decreased to \$0.3 million for the six months ended September 30, 2006 from \$4.2 million for the six months ended September 30, 2005, which included a gain of approximately \$2.2 million on the disposal of a subsidiary (see Note 11). The decrease in operating loss was due primarily to the increase in gross margin and the decrease in selling and marketing expenses.

*Selling and Marketing.* Selling and marketing expenses decreased by 13.5% to \$2.2 million in the second quarter of fiscal 2007 from \$2.5 million in the second quarter of fiscal 2006, primarily due to cost savings from the streamlining of logistics and warehousing, as well as the reorganization of the sales and marketing department.

Selling and marketing expenses decreased by 16.1% to \$4.4 million for the six months ended September 30, 2006 from \$5.3 million for the six months ended September 30, 2005, primarily due to the same reasons as the above.

*General and Administrative.* General and administrative expenses increased slightly to approximately \$1.7 million for the second quarter of fiscal 2007 compared to approximately \$1.6 million for the second quarter of fiscal 2006, primarily due to the expensing of non-cash share-based compensation in accordance to SFAS 123R (see Note 4).

General and administrative expenses remained steady at approximately \$3.3 million and \$3.4 million for the six months ended September 30, 2006 and 2005, respectively.

*Gain on disposal of a subsidiary.* We realized a net gain of approximately \$2.2 million in the first quarter of fiscal 2006 on the sale of a subsidiary, Warden Development Ltd. ( Warden ), which held title to an incomplete industrial building and the associated land use rights, located approximately three miles from our existing PRC production facilities. The incomplete industrial building was originally purchased with the intention of completing the facility for expansion of our existing production



facilities but this plan was subsequently aborted. The sale was completed on April 13, 2005, with full ownership of Warden and its associated risk transferred to the purchaser, for sales proceeds of approximately \$7.7 million in cash.

*Other Expenses net.* Other Expenses net primarily comprised losses from foreign currency transactions due to the relative strength or weakness of the US dollar at various times compared with the other currencies that we use to conduct our business.

*Interest Income.* Interest income increased by 47.3% to \$165,000 for the second quarter of fiscal 2007 from \$112,000 for the second quarter of fiscal 2006, primarily due to increase in bank deposit interest rates and increased cash placements in certificates of deposit yielding higher interest rates.

Interest income increased by 30.0% to \$282,000 for the six months ended September 30, 2006 from \$217,000 for the six months ended September 30, 2005, primarily due to increase in bank deposit interest rates and increased cash placements in certificates of deposit yielding higher interest rates.

*Income Tax Benefit.* Income tax benefit of \$103,000 was recorded for the second quarter of fiscal 2007, compared to an income tax benefit of \$91,000 recorded in the second quarter of fiscal 2006.

A \$21,000 tax benefit was recorded for the six months ended September 30, 2006, compared with a tax benefit of \$533,000 for the same period last year.

*Net Loss.* We had a net loss of approximately \$1.1 million for the second quarter of fiscal 2007, compared to a net loss of \$1.2 million for the same quarter of fiscal 2006, reflecting the effects of the previously discussed factors.

We had a net loss of \$0.2 million for the six months ended September 30, 2006, compared to a net loss of \$3.8 million for the six months ended September 30, 2005, as a result of the foregoing factors.

*Loss Per Share.* Diluted loss per share remained unchanged at \$0.09 for both the second quarter of fiscal 2007 and the same quarter last year, reflecting the effects of the foregoing factors.

Diluted loss per share for the six months ended September 30, 2006 was \$0.02, compared to a diluted loss per share of \$0.30 for the same period last year, reflecting the effects of the foregoing factors.

#### *Liquidity and Capital Resources*

Our net cash provided by operating activities was \$4.9 million for the six months ended September 30, 2006, compared to net cash used in operating activities of \$3.1 million for the six months ended September 30, 2005. This was primarily due to operating loss of \$0.3 million for the six months ended September 30, 2006 in comparison to operating loss of \$4.2 million for the six months ended September 30, 2005. The increase in cash provided by operating activities was also due to \$1.0 million of cash provided by accounts payable trade for the six months ended September 30, 2006 in comparison to \$3.8 million of cash used in accounts payable trade for the six months ended September 30, 2005.

Net cash used in investing activities was \$2.8 million for the six months ended September 30, 2006, compared to net cash provided by investing activities of \$0.2 million for the six months ended September 30, 2005. This was primarily due to increased acquisition of equipment during the six months ended September 30, 2006, and net proceeds on disposal of a subsidiary during the six months ended September 30, 2005.

No net cash was provided by nor used in financing activities for the six months ended September 30, 2006 and September 30, 2005 as there was no issuance or repurchase of common stock during these periods.

As of September 30, 2006, we had commitments for capital expenditures of \$0.2 million. The actual amounts of capital expenditures may vary substantially from those budgeted or estimated for a variety of reasons, including changes in market conditions, unavailability or changes in scheduled delivery of specific equipment, changes in interest rates and other factors. In addition, we plan to replace our obsolete fixed assets in future periods and plan to fund such replacements through our current cash reserves, future cash flow from operations and new bank borrowings as required.

As of September 30, 2006, we had no outstanding bank borrowings. Our principal source of liquidity consisted of \$19.5 million in cash and cash equivalents. We believe that our existing cash and cash equivalents and anticipated cash flow from operations will be sufficient to meet our anticipated cash needs in the ordinary course of business for at least the next 12 months. If our existing cash and cash equivalents and cash generated from operations are insufficient to satisfy our liquidity requirements, we may seek to sell additional public or private equity securities

or obtain debt financing. There can be no assurance that we will be able to sell additional equity securities, publicly or privately in the amounts that may be needed or at all.



There can be no assurance that additional financing will be available in the amounts that may be needed, or if available, will be obtained on terms favorable to us. Additional equity or debt financing may also be dilutive to our existing shareholders.

#### *Critical Accounting Policies*

In preparing our consolidated financial statements in conformity with accounting principles generally accepted in the United States of America, we must make a variety of estimates that affect the reported amounts and related disclosures. The following accounting policies are currently considered most critical to the preparation of our financial statements. If actual results differ significantly from management's estimates and projections, there could be a material effect on our financial statements.

*Share-Based Compensation.* As part of our adoption of SFAS 123R as of April 1, 2006, we were required to recognize the fair value of share-based compensation awards as an expense. We apply the Black-Scholes option-pricing model in order to determine the fair value of stock options on the date of grant, and we apply judgment in estimating key assumptions that are important elements in the model such as the expected stock-price volatility, expected stock option life and expected forfeiture ratios. Our estimates of these important assumptions are based on historical data and judgment regarding market trends and factors. If actual results are not consistent with our assumptions and judgments used in estimating these factors, we may be required to record additional share-based compensation expense, which could be material to our results of operations.

*Adoption of SFAS 123R.* In December 2004, the FASB issued SFAS 123R, which requires companies to measure and recognize compensation expense for all share-based payments at fair value. Share-based payments include stock options and non-vested share grants. We grant options to purchase common stock to some of our employees and directors under various plans at prices equal to the market value of the stock on the dates the options were granted. We historically have accounted for stock options using the method prescribed in APB 25 whereby stock options are granted at market price and no compensation cost is recognized, and disclosed the pro forma effect on net earnings assuming compensation cost had been recognized in accordance with SFAS 123. SFAS 123R, which was effective for us since April 1, 2006, eliminates the ability to account for share-based compensation transactions using APB 25, and generally requires that such transactions be accounted for using prescribed fair-value-based methods. SFAS 123R permits public companies to adopt its requirements using one of two methods: (a) a modified prospective method in which compensation costs are recognized beginning with the effective date based on the requirements of SFAS 123R for all share-based payments granted or modified after the effective date, and based on the requirements of SFAS 123 for all awards granted to employees prior to the effective date of SFAS 123R that remain unvested on the effective date or (b) a modified retrospective method which includes the requirements of the modified prospective method described above, but also permits companies to restate based on the amounts previously recognized under SFAS 123 for purposes of pro forma disclosures either for all periods presented or prior interim periods of the year of adoption. We have decided to adopt SFAS 123R using the modified prospective method.

*Revenue Recognition.* Our revenue is recognized when product has been shipped and title to the product has transferred to the customer. Title of the product may transfer to the end customer or distributor when shipped to or received by the customer based on the specific purchase terms of the agreement. We evaluate the provision for estimated returns monthly, based on historical sales and returns. To date we have not experienced significant returns. Any increase in the level of returns could have a material and adverse effect on our financial statements.

*Allowance for Doubtful Accounts.* Allowance for doubtful accounts is made against accounts receivable to the extent they are considered to be doubtful of collection. Accounts receivable in the balance sheet are stated net of such provision. We evaluate the collectability of our accounts receivable based on a combination of factors. In circumstances where we are aware of a specific customer's inability to meet its financial obligation to us, we record a specific reserve for bad debts against amounts due. A provision is also made based on the aging of the receivables. If circumstances change, such as the incurrence of higher than expected defaults or an unexpected material adverse change occurs regarding a major customer's ability to meet its financial obligations to us, our estimates of the recoverability of amounts due to us could be reduced by a material amount.

*Inventory Valuation.* We write down our inventory for estimated obsolescence or unmarketable inventory equal to the difference between the cost of inventory and the estimated market value based upon assumptions about future demand and market conditions. At each balance sheet date, inventory on hand in excess of one year's demand or usage or those that were produced more than twelve months ago, are written down to zero. If actual future demand or market conditions are less favorable than those projected by management, additional write-downs may be required.

*Valuation of Long-lived Assets.* We assess the carrying value of long-lived assets whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Factors we consider important which could trigger an impairment review include the following:

significant under-performance relative to expected historical or projected future operating results;

significant changes in the manner of our use of the asset;

significant negative industry or economic trends; and

our market capitalization relative to net book value.

Upon the existence of one or more of the above indicators of impairment, we test such assets for a potential impairment. The carrying value of a long-lived asset is considered impaired when the estimated future cash flows, undiscounted, are less than the asset's carrying value. In that event, a loss is recognized based on the amount by which the carrying value exceeds the fair market value of the long-lived asset. Fair market value is determined primarily using the anticipated cash flows discounted at a rate commensurate with the risk involved.

*Deferred Taxes.* As part of the process of preparing our consolidated financial statements, we are required to estimate our income taxes and tax bases of assets and liabilities in each of the jurisdictions in which we operate. This process involves us estimating our current tax exposure together with assessing temporary differences resulting from differing treatment of items for tax and accounting purposes. These differences result in deferred tax assets and liabilities, which are included in our consolidated balance sheet. We must then assess the likelihood that our deferred tax assets will be recovered from future taxable income, and, to the extent we believe that recovery is more unlikely than likely, we must establish a valuation allowance. To the extent we establish a valuation allowance or increase this allowance in a period, we must include an expense within the tax provision in the statement of operations. Any change in the future recoverability of the deferred tax assets could significantly affect the results of our operations or cash flows.

*Property, plant and equipment, net.* Property, plant and equipment is stated at cost less accumulated depreciation. Gains or losses on disposals are reflected in current operations. Major expenditures for betterments and renewals are capitalized. All ordinary repairs and maintenance costs are expensed as incurred. Depreciation is provided using the straight-line method over the estimated useful lives.

The useful lives of property, plant and equipment adopted for depreciation purposes are as follows:

Buildings	10 years
Plant, machinery and equipment	5-10 years
Molds	3-5 years
Leasehold improvements, furniture, fixtures and motor vehicles	5-10 years

**Item 3. Quantitative and Qualitative Disclosures about Market Risk**

*Currency Exchange Rate Fluctuations*

Our sales are denominated primarily in US dollars while our cost of goods sold are generally incurred in US dollars, Hong Kong dollars and Renminbi, and our operating expenses are generally denominated in Renminbi, Hong Kong dollars, Singapore dollars, New Taiwanese dollars and US dollars. In addition, a substantial portion of our capital expenditures, primarily for the purchase of equipment, has been and is expected to continue to be denominated in US dollars, Renminbi, Japanese Yen and the Euro. Consequently, a portion of our costs and operating margins may be affected by fluctuations in exchange rates, primarily between the US dollar and other currencies. Our results of operations and financial condition could be adversely affected by fluctuations in currency exchange rates or the imposition of new or additional currency controls in the jurisdictions in which we operate. At September 30, 2006 and 2005, we had no outstanding foreign exchange contracts.

As the Hong Kong dollar is officially pegged to the US dollar and the Renminbi is controlled by the PRC government such that it only trades within a limited range against the US dollar, unless there are significant changes in the policies of the Hong Kong and the PRC government, fluctuations in the exchange rates of the Hong Kong dollar and the Renminbi are not expected to have a significant impact on our results of operations. However, should the PRC government allow the Renminbi to have a wider trading range, resulting in a significant appreciation of the Renminbi against the US dollar, our production costs will increase and our operating margins will erode.

**Item 4. Controls and Procedures**

(a) **Evaluation of disclosure controls and procedures.** We maintain disclosure controls and procedures, as such term is defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (the Exchange Act), that are designed to ensure that information required to be disclosed by us in reports that we file or submit under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in Securities and Exchange Commission rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure. In designing and evaluating our disclosure controls and procedures, management recognized that disclosure controls and procedures, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the disclosure controls and procedures are met. Our disclosure controls and procedures have been designed to meet reasonable assurance standards. Additionally, in designing disclosure controls and procedures, our management necessarily was required to apply its judgment in evaluating the cost-benefit relationship of possible disclosure controls and procedures. The design of any disclosure controls and procedures also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions.

Based on their evaluation as of the end of the period covered by this Quarterly Report on Form 10-Q, our Chief Executive Officer and Chief Financial Officer have concluded that, as of such date, our disclosure controls and procedures were effective at the reasonable assurance level.

(b) **Changes in internal control over financial reporting.** There was no significant change in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) identified in connection with management's evaluation during the last fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

**PART II**

**OTHER INFORMATION**

**Item 1. Legal Proceedings**

See Note 9, Commitments and Contingencies, of our unaudited condensed consolidated financial statements contained in Part I of this Quarterly Report on Form 10-Q.

**Item 1A. Risk Factors**

The following risk factors supplement the Risk Factors disclosed in our Annual Report on Form 10-K for the fiscal year ended March 31, 2006 as filed with the Securities and Exchange Commission on June 29, 2006:

*Our operating results are difficult to predict and are likely to fluctuate significantly based on several factors, which can cause our stock price to decline.*

Our operating results are affected by a wide variety of factors that could materially affect net sales and profitability or lead to significant fluctuations in our quarterly or annual operating results. These factors include, among others:

the price of raw materials, the majority of which are petroleum derivatives. Prices of these raw materials are significantly affected by oil prices which recently have become volatile;

our ability to reduce the high materials cost of our products;

factors relating to conditions in the semiconductor, disk drive and electronic industries including:

lower demand for products;

increased price competition;

downturns and deterioration of business conditions;

technological changes and the introduction of new products;

changes in production processes in the semiconductor and electronic industries which could require changes in packaging products; and

consolidation among our customers, which may lead to reduced sales for us.

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although we do not believe that it is our liability, the need for us to pay and the amounts that we might pay on a voluntary basis for certain tax, social insurance contributions and potential penalties on behalf of the factory at which our products are manufactured in order to avoid the seizure of the factory's assets and keep it operational, as well as claims resulting from employee lawsuits against the factory;

capital requirements and the availability of funding;

inability or difficulty in meeting new or exacting product specifications from customers

our expansion plan and possible disruptions caused by the installation of new equipment or the construction of new facilities;

difficulties in recycling trays manufactured using our proprietary plastic compounds;

the lack of long-term purchase or supply agreements with customers;

the loss of key personnel or the shortage of available skilled employees;

international political or economic events or developments, including those relating to Hong Kong and the PRC;

our relationship with our processing partner in the PRC and the ability of the government of the PRC to seize the assets and shut down our factory operated in the PRC;

production volume fluctuations and the management of our inventories;

currency fluctuations and foreign exchange rules and regulations in the PRC;

the recurrence of SARS or other major health issues in Asia;

the outcome of patent litigation in Taiwan; and

the imposition of fines, penalties and bonds arising from violations of rules and regulations in the PRC relating to customs regulations, foreign currency exchange rules, taxation, the withholding of taxes for employees and other laws and regulation.

Unfavorable changes in the above or other factors could substantially harm our results of operations or financial condition. We believe that period to period comparisons of our results of operations will not necessarily be meaningful. You should not rely on these comparisons as an indication of our future performance. If our results of operations in one or more periods fail to meet or exceed the expectations of securities analysts or investors, the trading price of our common stock may decline, possibly by a significant amount.

*Failure to successfully defend against intellectual property lawsuits brought against us may adversely affect our business.*

As technology is an integral part of our design and product, we have, in the past, received communications alleging that our products infringe or misappropriate certain intellectual property rights held by others, and may continue to receive such communications in the future. We are currently involved in an intellectual property dispute with R.H. Murphy Co., Inc. See Part II, Item 1. Legal Proceedings. If any third party were to make valid intellectual property infringement or misappropriation claims against us, we may be required to:

discontinue using disputed manufacturing process technologies;

stop selling products that contain allegedly infringing technology;

pay substantial monetary damages;

seek to develop non-infringing technologies, which may not be feasible; or

seek to acquire licenses to the infringed technology, which may not be available on commercially reasonable terms, if at all.

If our products are found to infringe or misappropriate third-party intellectual property rights, we may be subject to significant liabilities and be required to change our manufacturing processes or products. This could restrict us from making, using, selling or exporting some of our products, which could in turn materially and adversely affect our business and financial condition. Our failure to develop non-infringing technologies or license intellectual property rights in a timely and cost-effective manner could materially and adversely affect our business and financial condition. In addition, any litigation, whether to enforce our patents or other intellectual property rights or to defend ourselves against claims that we have infringed the intellectual property rights of others, could, regardless of the ultimate outcome, materially and adversely affect our operating results by requiring us to incur significant legal expenses and diverting the resources of the company and the attention of management.

*The loss of any of our key personnel or the failure to attract or retain specialized technical and management personnel could impair our ability to grow our business.*

We rely heavily on the services of our key employees such as (i) Dean Personne, our Chief Executive Officer, (ii) John Supan, our Chief Financial Officer, (iii) Splendid Zuo, our Vice President, General Manager of Operations, (iv) Mary Chow, our Vice President, Supply Chain Management, and (v) Chris Buckley, our Vice President, Southeast Asia Sales. We believe our future success will depend upon our ability to retain these and other key employees and our ability to attract and retain other skilled managerial, engineering, technical and sales and marketing personnel. For instance, in September 2006, we parted company with our senior vice president of sales. The competition for such personnel, particularly management and technical personnel, is intense in our industry. Despite the incentives we provide, our current employees may not continue to work for us, and if additional personnel were required for our operations, we may not be able to obtain the services of additional personnel necessary for our growth. The loss of any of our key employees or our inability to attract or retain qualified personnel, including engineers, could delay the development and introduction of and have an adverse effect on our ability to sell, our products as well as our overall growth.

*We may engage in future acquisitions and we may be unable to successfully integrate these companies into our operations, which would adversely affect our business.*

As part of our growth strategy, we may make acquisitions and investments in companies or businesses. The success of our acquisitions and investments depends on a number of factors, including:



our ability to identify suitable opportunities for investment or acquisition;

our ability to reach an acquisition or investment agreement on terms that are satisfactory to us or at all;

the extent to which we are able to exercise control over the acquired company;

the economic, business or other strategic objectives and goals of the acquired company compared to those of our company; and

our ability to successfully integrate the acquired company or business with our company.

If we are unsuccessful in our acquisitions, we may not be able to implement fully our business strategy to maintain or grow our business.

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

Not applicable.

**Item 3. Defaults Upon Senior Securities**

Not applicable.

**Item 4. Submission of Matters to a Vote of Security Holders**

Not applicable.

**Item 5. Other Information**

Not applicable.

**Item 6. Exhibits**

- 10.1 Employment Agreement, dated August 1, 2006, by and between the Company and John Supan (incorporated by reference to Exhibit 10.1 to the Company's Current Report on Form 8-K, dated August 1, 2006 and filed on August 3, 2006)
- 10.2 Addendum to Employment Agreement by and between the Company and Dean Personne (incorporated by reference to Exhibit 99.1 to the Company's Current Report on Form 8-K, dated August 25, 2006 and filed on August 29, 2006)
- 10.3 Addendum to Employment Agreement by and between the Company and Michael Bingham (incorporated by reference to Exhibit 99.1 to the Company's Current Report on Form 8-K, dated August 25, 2006 and filed on August 29, 2006)
- 31.1 Rule 13a-14(a) Certification by the Chief Executive Officer
- 31.2 Rule 13a-14(a) Certification by the Chief Financial Officer
- 32.1 Section 1350 Certification by the Chief Executive Officer
- 32.2 Section 1350 Certification by the Chief Financial Officer

**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.

PEAK INTERNATIONAL LIMITED

Date: November 9, 2006

By */s/* Dean Personne  
**Dean Personne**  
**President and Chief Executive Officer**

Date: November 9, 2006

By */s/* John Supan  
**John Supan**  
**Chief Financial Officer**

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