

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

FORM 10-Q

(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended June 30, 2020**

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: 001-35435

Proto Labs, Inc.

(Exact name of registrant as specified in its charter)

Minnesota

(State or other jurisdiction of incorporation or organization)

41-1939628

(I.R.S. Employer Identification No.)

**5540 Pioneer Creek Drive
Maple Plain, Minnesota**

(Address of principal executive offices)

55359

(Zip Code)

(763) 479-3680

(Registrant's telephone number, including area code)

Not Applicable

(Former name, former address and former fiscal year, if changed since last report)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Trading Symbol(s)	Name of each exchange on which registered
Common Stock, Par Value \$0.001 Per Share	PRLB	New York Stock Exchange

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter 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 has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer
Non-accelerated filer
Smaller reporting company Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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: 26,706,556 shares of Common Stock, par value \$0.001 per share, were outstanding at July 28, 2020.

Proto Labs, Inc.
TABLE OF CONTENTS

Item	Description	Page
<u>PART I</u>		
1.	Financial Statements	2
2.	Management's Discussion and Analysis of Financial Condition and Results of Operations	16
3.	Quantitative and Qualitative Disclosures about Market Risk	26
4.	Controls and Procedures	27
<u>PART II</u>		
1.	Legal Proceedings	28
1A.	Risk Factors	28
2.	Unregistered Sales of Equity Securities and Use of Proceeds	28
3.	Defaults Upon Senior Securities	28
4.	Mine Safety Disclosures	28
5.	Other Information	28
6.	Exhibits	29

PART I. FINANCIAL INFORMATION**Item 1. Financial Statements**

Proto Labs, Inc.
Consolidated Balance Sheets
(In thousands, except share and per share amounts)

	June 30, 2020 (Unaudited)	December 31, 2019
Assets		
Current assets		
Cash and cash equivalents	\$ 98,003	\$ 125,225
Short-term marketable securities	33,128	35,437
Accounts receivable, net of allowance for doubtful accounts of \$1,836 and \$952 as of June 30, 2020 and December 31, 2019, respectively	61,297	57,450
Inventory	10,774	10,075
Income taxes receivable	95	-
Prepaid expenses and other current assets	9,670	8,232
Total current assets	212,967	236,419
Property and equipment, net	281,129	263,712
Goodwill	128,752	128,752
Other intangible assets, net	15,861	17,369
Long-term marketable securities	44,127	12,960
Operating lease assets	11,049	11,425
Other long-term assets	4,560	3,030
Total assets	\$ 698,445	\$ 673,667
Liabilities and shareholders' equity		
Current liabilities		
Accounts payable	\$ 17,556	\$ 16,804
Accrued compensation	15,138	15,058
Accrued liabilities and other	15,041	11,057
Current operating lease liabilities	3,368	3,340
Income taxes payable	-	1,322
Total current liabilities	51,103	47,581
Long-term operating lease liabilities	8,379	8,565
Long-term deferred tax liabilities	31,907	26,283
Other long-term liabilities	5,807	5,448
Total liabilities	97,196	87,877
Shareholders' equity		
Preferred stock, \$0.001 par value, authorized 10,000,000 shares; issued and outstanding 0 shares as of each of June 30, 2020 and December 31, 2019	-	-

Common stock, \$0.001 par value, authorized 150,000,000 shares; issued and outstanding 26,706,556 and 26,786,459 shares as of June 30, 2020 and December 31, 2019, respectively	27	27
Additional paid-in capital	272,231	268,059
Retained earnings	338,625	324,722
Accumulated other comprehensive loss	(9,634)	(7,018)
Total shareholders' equity	601,249	585,790
Total liabilities and shareholders' equity	\$ 698,445	\$ 673,667

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

2

[Table of Contents](#)

Proto Labs, Inc.
Consolidated Statements of Comprehensive Income
(In thousands, except share and per share amounts)
(Unaudited)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2020	2019	2020	2019
Statements of Operations:				
Revenue	\$ 106,575	\$ 115,932	\$ 221,683	\$ 229,384
Cost of revenue	54,119	55,696	111,127	110,288
Gross profit	52,456	60,236	110,556	119,096
Operating expenses				
Marketing and sales	16,936	19,285	35,116	37,862
Research and development	8,648	8,169	17,635	16,182
General and administrative	12,521	13,209	26,629	26,031
Total operating expenses	38,105	40,663	79,380	80,075
Income from operations	14,351	19,573	31,176	39,021
Other income, net	767	1,125	1,821	1,338
Income before income taxes	15,118	20,698	32,997	40,359
Provision for income taxes	2,511	4,532	6,406	8,682
Net income	\$ 12,607	\$ 16,166	\$ 26,591	\$ 31,677
Net income per share:				
Basic	\$ 0.47	\$ 0.60	\$ 1.00	\$ 1.18
Diluted	\$ 0.47	\$ 0.60	\$ 0.99	\$ 1.17
Shares used to compute net income per share:				
Basic	26,660,498	26,875,153	26,718,652	26,919,016
Diluted	26,760,866	27,041,422	26,837,938	27,113,328
Comprehensive Income (net of tax)				
Comprehensive income	\$ 12,971	\$ 15,688	\$ 23,975	\$ 31,675

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

3

[Table of Contents](#)

Proto Labs, Inc.
Consolidated Statements of Shareholders' Equity
(In thousands, except share amounts)

Common Stock		Additional Paid-In Capital	Retained Earnings	Accumulated Other Comprehensive Loss	Total
Shares	Amount				

Balance at January 1, 2020	26,786,459	27	268,059	324,722	(7,018)	585,790
Common shares issued on exercise of options and other, net of shares withheld for tax obligations	23,525	-	(902)	-	-	(902)
Stock-based compensation expense	-	-	3,033	-	-	3,033
Repurchases of common stock	(161,460)	-	(1,616)	(9,569)	-	(11,185)
Net income	-	-	-	13,984	-	13,984
<i>Other comprehensive income</i>						
Foreign currency translation adjustment	-	-	-	-	(2,980)	(2,980)
Comprehensive income						11,004
Balance at March 31, 2020	<u>26,648,524</u>	<u>\$ 27</u>	<u>\$ 268,574</u>	<u>\$ 329,137</u>	<u>\$ (9,998)</u>	<u>\$ 587,740</u>
Common shares issued on exercise of options and other, net of shares withheld for tax obligations	96,186	-	400	-	-	400
Stock-based compensation expense	-	-	3,639	-	-	3,639
Repurchases of common stock	(38,154)	-	(382)	(3,119)	-	(3,501)
Net income	-	-	-	12,607	-	12,607
<i>Other comprehensive income</i>						
Foreign currency translation adjustment	-	-	-	-	364	364
Comprehensive income						12,971
Balance at June 30, 2020	<u>26,706,556</u>	<u>\$ 27</u>	<u>\$ 272,231</u>	<u>\$ 338,625</u>	<u>\$ (9,634)</u>	<u>\$ 601,249</u>
			Common Stock	Additional	Retained	Accumulated
			Shares	Paid-In	Earnings	Other
			Amount	Capital		Comprehensive
						Loss
						Total
Balance at January 1, 2019	26,984,747	27	258,502	291,460	(8,492)	541,497
Common shares issued on exercise of options and other, net of shares withheld for tax obligations	19,950	-	(420)	-	-	(420)
Stock-based compensation expense	-	-	3,040	-	-	3,040
Repurchases of common stock	(157,716)	-	(1,511)	(15,798)	-	(17,309)
Net income	-	-	-	15,511	-	15,511
<i>Other comprehensive income</i>						
Foreign currency translation adjustment	-	-	-	-	476	476
Comprehensive income						15,987
Balance at March 31, 2019	<u>26,846,981</u>	<u>\$ 27</u>	<u>\$ 259,611</u>	<u>\$ 291,173</u>	<u>\$ (8,016)</u>	<u>\$ 542,795</u>
Common shares issued on exercise of options and other, net of shares withheld for tax obligations	75,785	-	245	-	-	245
Stock-based compensation expense	-	-	3,486	-	-	3,486
Repurchases of common stock	(40,669)	-	(390)	(3,711)	-	(4,101)
Net income	-	-	-	16,166	-	16,166
<i>Other comprehensive income</i>						
Foreign currency translation adjustment	-	-	-	-	(478)	(478)
Comprehensive income						15,688
Balance at June 30, 2019	<u>26,882,097</u>	<u>\$ 27</u>	<u>\$ 262,952</u>	<u>\$ 303,628</u>	<u>\$ (8,494)</u>	<u>\$ 558,113</u>

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

[Table of Contents](#)

Proto Labs, Inc.
Consolidated Statements of Cash Flows
(In thousands)
(Unaudited)

	Six Months Ended	
	June 30,	
	2020	2019
Operating activities		
Net income	\$ 26,591	\$ 31,677
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	15,855	14,981
Stock-based compensation expense	6,672	6,526
Deferred taxes	5,651	1,585
Amortization of held-to-maturity securities	129	7
Other	(854)	(279)
Changes in operating assets and liabilities:		

Accounts receivable	(4,292)	(3,461)
Inventories	(801)	392
Prepaid expenses and other	(1,068)	24
Income taxes	(1,341)	4,833
Accounts payable	1,082	3,848
Accrued liabilities and other	5,793	(5,245)
Net cash provided by operating activities	53,417	54,888
Investing activities		
Purchases of property, equipment and other capital assets	(33,305)	(34,136)
Purchases of other assets and investments	(3,000)	(4,000)
Purchases of marketable securities	(57,212)	(8,983)
Proceeds from maturities of marketable securities	28,225	29,170
Net cash used in investing activities	(65,292)	(17,949)
Financing activities		
Proceeds from exercises of stock options	2,855	2,243
Purchases of shares withheld for tax obligations	(3,367)	(2,418)
Repurchases of common stock	(14,686)	(21,410)
Net cash used in financing activities	(15,198)	(21,585)
Effect of exchange rate changes on cash and cash equivalents	(149)	135
Net (decrease) increase in cash and cash equivalents	(27,222)	15,489
Cash and cash equivalents, beginning of period	125,225	85,046
Cash and cash equivalents, end of period	\$ 98,003	\$ 100,535

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

[Table of Contents](#)

Note 1 – Basis of Presentation

The unaudited interim Consolidated Financial Statements of Proto Labs, Inc. (ProtoLabs, the Company, we, us or our) have been prepared in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, the accompanying financial statements reflect all adjustments necessary for a fair presentation of the Company's statements of financial position, results of operations and cash flows for the periods presented. Except as otherwise disclosed herein, these adjustments consist of normal, recurring items. Operating results for interim periods are not necessarily indicative of results that may be expected for the fiscal year as a whole.

The preparation of the financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues, expenses, and the related disclosures at the date of the financial statements and during the reporting period. Actual results could materially differ from these estimates. For further information, refer to the audited Consolidated Financial Statements and Notes thereto included in the Company's Annual Report on Form 10-K for the year ended December 31, 2019 as filed with the Securities and Exchange Commission (SEC) on February 26, 2020.

The accompanying Consolidated Balance Sheet as of December 31, 2019 was derived from the audited Consolidated Financial Statements but does not include all disclosures required by U.S. GAAP for a full set of financial statements. This Form 10-Q should be read in conjunction with the Company's Consolidated Financial Statements and Notes included in the Annual Report on Form 10-K filed on February 26, 2020 as referenced above.

Note 2 – Recent Accounting Pronouncements

Recently Adopted Accounting Pronouncements

During the first quarter of 2020, the Company adopted the Financial Accounting Standards Board (FASB) Accounting Standards Update (ASU) 2016-13, *Financial Instruments – Credit Losses*, which is intended to provide financial statement users with more decision-useful information about the expected credit losses on financial instruments held by a reporting entity at each reporting date. The adoption of this guidance had no material impact on our consolidated financial statements.

During the fourth quarter of 2019, the Company early adopted the FASB ASU 2017-04, *Intangibles – Goodwill and Other*, which is intended to simplify the subsequent measurement of goodwill. The adoption of this guidance had no material impact on our consolidated financial statements.

Note 3 – Net Income per Common Share

Basic net income per share is computed based on the weighted-average number of common shares outstanding. Diluted net income per share is computed based on the weighted-average number of common shares outstanding, increased by the number of additional shares that would have been outstanding had potentially dilutive common shares been issued and reduced by the number of shares the Company could have repurchased from the proceeds from issuance of the potentially dilutive shares. Potentially dilutive shares of common stock include stock options, restricted stock units and restricted stock awards granted under stock-based compensation plans and shares committed to be purchased under the employee stock purchase plan. Performance stock units are excluded from the calculation of dilutive potential common shares until the performance conditions have been satisfied.

The table below sets forth the computation of basic and diluted net income per share:

(in thousands, except share and per share amounts)	Three Months Ended June 30,		Six Months Ended June 30,	
	2020	2019	2020	2019
Net income	\$ 12,607	\$ 16,166	\$ 26,591	\$ 31,677
Basic - weighted-average shares outstanding:	26,660,498	26,875,153	26,718,652	26,919,016
Effect of dilutive securities:				
Employee stock options and other	100,368	166,269	119,286	194,312
Diluted - weighted-average shares outstanding:	26,760,866	27,041,422	26,837,938	27,113,328
Net income per share:				
Basic	\$ 0.47	\$ 0.60	\$ 1.00	\$ 1.18
Diluted	\$ 0.47	\$ 0.60	\$ 0.99	\$ 1.17

Note 4 – Goodwill and Other Intangible Assets

There were no changes in the carrying amount of Goodwill during the three and six months ended June 30, 2020.

Intangible assets other than goodwill at June 30, 2020 and December 31, 2019 were as follows:

(in thousands)	June 30, 2020			December 31, 2019			Useful Life (in years)	Weighted Average Useful Life Remaining (in years)
	Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net		
Intangible assets with finite lives:								
Marketing assets	\$ 930	\$ (574)	\$ 356	\$ 930	\$ (527)	\$ 403	10.0	3.8
Non-compete agreement	270	(230)	40	270	(222)	48	2.0 - 5.0	2.5
Software technology	13,229	(2,960)	10,269	13,229	(2,275)	10,954	10.0	7.5
Customer relationships	10,070	(4,874)	5,196	10,070	(4,106)	5,964	6.0 - 9.0	3.3
Total intangible assets	\$ 24,499	\$ (8,638)	\$ 15,861	\$ 24,499	\$ (7,130)	\$ 17,369		

Amortization expense for intangible assets was \$0.8 million and \$0.9 million for the three months ended June 30, 2020 and 2019, respectively, and \$1.5 million and \$1.7 million for the six months ended June 30, 2020 and 2019, respectively.

Estimated aggregated amortization expense based on the current carrying value of the amortizable intangible assets is as follows:

(in thousands)	Estimated Amortization Expense
Remaining 2020	\$ 1,508
2021	3,016
2022	3,016
2023	2,813
2024	1,400
Thereafter	4,108
Total estimated amortization expense	\$ 15,861

Note 5 – Fair Value Measurements

Accounting Standards Codification (ASC 820), *Fair Value Measurement* (ASC 820), defines fair value as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. ASC 820 also establishes a fair value hierarchy that requires classification based on observable and unobservable inputs when measuring fair value. There are three levels of inputs that may be used to measure fair value:

Level 1—Quoted prices in active markets for identical assets or liabilities.

Level 2—Observable inputs other than Level 1 prices such as quoted prices for similar assets or liabilities; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities.

Level 3—Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets or liabilities.

The Company's cash consists of bank deposits. The Company's cash equivalents measured at fair value consist of money market mutual funds. The Company determines the fair value of these investments using Level 1 inputs.

The following table summarizes financial assets as of June 30, 2020 and December 31, 2019 measured at fair value on a recurring basis:

(in thousands)	June 30, 2020			December 31, 2019		
	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Financial Assets:						
Cash and cash equivalents						
Money market mutual fund	\$ 26,088	\$ -	\$ -	\$ 68,962	\$ -	\$ -
Total	<u>\$ 26,088</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 68,962</u>	<u>\$ -</u>	<u>\$ -</u>

Note 6 – Marketable Securities

The Company invests in short-term and long-term agency, municipal, corporate and other debt securities. The securities are categorized as held-to-maturity and are recorded at amortized cost, net of an allowance for credit losses. Categorization as held-to-maturity is based on the Company's ability and intent to hold these securities to maturity. The following table summarizes information regarding the Company's short-term and long-term marketable securities as of June 30, 2020 and December 31, 2019:

(in thousands)	June 30, 2020			
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. municipal securities	\$ 8,840	\$ 71	\$ -	\$ 8,911
Corporate debt securities	34,968	355	(2)	35,321
U.S. government agency securities	25,272	23	(5)	25,290
Certificates of deposit/time deposits	5,189	112	-	5,301
Commercial paper	2,986	13	-	2,999
Total marketable securities	<u>\$ 77,255</u>	<u>\$ 574</u>	<u>\$ (7)</u>	<u>\$ 77,822</u>

(in thousands)	December 31, 2019			
	Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. municipal securities	\$ 10,204	\$ 9	\$ (3)	\$ 10,210
Corporate debt securities	26,944	80	(12)	27,012
U.S. government agency securities	6,274	1	(7)	6,268
Certificates of deposit/time deposits	1,484	22	-	1,506
Commercial paper	3,491	-	-	3,491
Total marketable securities	<u>\$ 48,397</u>	<u>\$ 112</u>	<u>\$ (22)</u>	<u>\$ 48,487</u>

Fair values for the corporate debt securities are primarily determined based on quoted market prices (Level 1). Fair values for the U.S. municipal securities, U.S. government agency securities, certificates of deposit and U.S. treasury securities are primarily determined using dealer quotes or quoted market prices for similar securities (Level 2).

During the first quarter of 2020, the Company adopted the FASB ASU 2016-13, *Financial Instruments – Credit Losses*. The Company calculated the expected credit loss for each security in its portfolio using the probability-of-default method. The Company concluded the adoption of the guidance had no material impact on its consolidated financial statements.

Classification of marketable securities as current or non-current is based upon the security’s maturity date as of the date of these financial statements.

The June 30, 2020 balance of held-to-maturity debt securities by contractual maturity is shown in the following table at amortized cost, net of an allowance for credit losses. Actual maturities may differ from contractual maturities because the issuers of the securities may have the right to prepay obligations without prepayment penalties.

(in thousands)	June 30, 2020
Due in one year or less	\$ 33,128
Due after one year through five years	44,127
Total marketable securities	\$ 77,255

Note 7 – Inventory

Inventory consists primarily of raw materials, which are recorded at the lower of cost or market using the average-cost method, which approximates first-in, first-out (FIFO) cost. The Company periodically reviews its inventory for slow-moving, damaged and discontinued items and provides allowances to reduce such items identified to their recoverable amounts.

The Company’s inventory consisted of the following as of the dates indicated:

(in thousands)	June 30, 2020	December 31, 2019
Raw materials	\$ 10,784	\$ 9,818
Work in process	228	501
Total inventory	11,012	10,319
Allowance for obsolescence	(238)	(244)
Inventory, net of allowance	\$ 10,774	\$ 10,075

[Table of Contents](#)

Note 8 – Stock-Based Compensation

Under the Company’s 2012 Long-Term Incentive Plan, as amended (the 2012 Plan), the Company has the ability to grant stock options, stock appreciation rights (SARs), restricted stock, restricted stock units, other stock-based awards and cash incentive awards. Awards under the 2012 Plan have a maximum term of ten years from the date of grant. The compensation committee may provide that the vesting or payment of any award will be subject to the attainment of specified performance measures in addition to the satisfaction of any continued service requirements and the compensation committee will determine whether such measures have been achieved. The per-share exercise price of stock options and SARs granted under the 2012 Plan generally may not be less than the fair market value of a share of our common stock on the date of the grant.

Employee Stock Purchase Plan

The Company’s 2012 Employee Stock Purchase Plan (ESPP) allows eligible employees to purchase a variable number of shares of the Company’s common stock each offering period at a discount through payroll deductions of up to 15 percent of their eligible compensation, subject to plan limitations. The ESPP provides for six-month offering periods with a single purchase period ending May 15 and November 15, respectively. At the end of each offering period, employees are able to purchase shares at 85 percent of the lower of the fair market value of the Company’s common stock on the first trading day of the offering period or on the last trading day of the offering period.

Stock-Based Compensation Expense

Stock-based compensation expense was \$3.6 million and \$3.5 million for the three months ended June 30, 2020 and 2019, respectively, and \$6.7 million and \$6.5 million for the six months ended June 30, 2020 and 2019, respectively.

Stock Options

The following table summarizes stock option activity during the six months ended June 30, 2020:

	Stock Options	Weighted-Average Exercise Price
Options outstanding at December 31, 2019	276,266	\$ 72.38
Granted	60,065	105.79
Exercised	(18,052)	49.68
Forfeited	(36,841)	66.97
Options outstanding at June 30, 2020	<u>281,438</u>	<u>\$ 81.67</u>
Exercisable at June 30, 2020	<u>144,822</u>	<u>\$ 65.88</u>

The outstanding options generally have a term of ten years. For employees, options granted become exercisable ratably over the vesting period, which is generally a period from four to five years, beginning on the first anniversary of the grant date, subject to the employee's continuing service to the Company. For directors, options generally become exercisable in full on the first anniversary of the grant date.

The weighted-average grant date fair value of options that were granted during the six months ended June 30, 2020 was \$45.32.

The following table provides the assumptions used in the Black-Scholes pricing model valuation of options during the six months ended June 30, 2020 and 2019:

	Six Months Ended June 30,	
	2020	2019
Risk-free interest rate	0.50 - 1.47%	2.35 - 2.58%
Expected life (years)	6.25	6.25
Expected volatility	42.40 - 43.83%	42.52 - 42.74%
Expected dividend yield	0%	0%

As of June 30, 2020, there was \$5.3 million of unrecognized compensation expense related to unvested stock options, which is expected to be recognized over a weighted-average period of 3.0 years.

[Table of Contents](#)

Restricted Stock

Restricted stock awards are share-settled awards and restrictions lapse ratably over the vesting period, which is generally a period from four to five years, beginning on the first anniversary of the grant date, subject to the employee's continuing service to the Company. For directors, restrictions generally lapse in full on the first anniversary of the grant date.

The following table summarizes restricted stock activity during the six months ended June 30, 2020:

	Restricted Stock	Weighted-Average Grant Date Fair Value Per Share
Restricted stock at December 31, 2019	314,973	\$ 89.55
Granted	107,988	111.72
Restrictions lapsed	(100,596)	84.57
Forfeited	(9,253)	91.25
Restricted stock at June 30, 2020	<u>313,112</u>	<u>\$ 98.75</u>

As of June 30, 2020, there was \$27.4 million of unrecognized compensation expense related to non-vested restricted stock, which is expected to be recognized over a weighted-average period of 2.8 years.

Performance Stock

Performance stock units (PSUs) are expressed in terms of a target number of PSUs, with anywhere between 0 percent and 150 percent of that target number capable of being earned and vesting at the end of a three-year performance period depending on the Company's performance in the final year of the performance period and the award recipient's continued employment. The Company's PSUs granted from 2017 to 2019 are based on performance conditions and the related compensation cost is based on the probability that the performance conditions will be achieved. The Company's PSUs granted in 2020 are based on market conditions and the related compensation cost is based on the fair value at grant date calculated using a Monte Carlo pricing model.

The following table summarizes performance stock activity during the six months ended June 30, 2020:

	Performance Stock	Weighted- Average Grant Date Fair Value Per Share
Performance stock at December 31, 2019	9,383	\$ 58.35
Granted	19,956	118.66
Restrictions lapsed	(7,113)	58.35
Performance change	-	-
Forfeited	(2,270)	58.35
Performance stock at June 30, 2020	<u>19,956</u>	<u>\$ 118.66</u>

The following table provides the assumptions used in the Monte Carlo pricing model valuation of PSUs during the six months ended June 30, 2020:

	Six Months Ended June 30, 2020
Risk-free interest rate	1.41%
Expected life (years)	2.88
Expected volatility	38.70%
Expected dividend yield	0%

As of June 30, 2020, there was \$2.1 million of unrecognized compensation expense related to non-vested performance stock, which is expected to be recognized over a weighted-average period of 2.6 years.

Employee Stock Purchase Plan

The following table presents the assumptions used to estimate the fair value of the ESPP during the six months ended June 30, 2020 and 2019:

	Six Months Ended June 30,	
	2020	2019
Risk-free interest rate	0.17 - 1.59%	2.33 - 2.35%
Expected life (months)	6.00	6.00
Expected volatility	42.63 - 59.99%	37.36 - 53.57%
Expected dividend yield	0%	0%

Note 9 – Accumulated Other Comprehensive Loss

Other comprehensive income (loss) is comprised entirely of foreign currency translation adjustments. The following table presents the changes in accumulated other comprehensive income (loss) balances during the three and six months ended June 30, 2020 and 2019:

(in thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2020	2019	2020	2019

Foreign currency translation adjustments								
Balance at beginning of period	\$	(9,998)	\$	(8,016)	\$	(7,018)	\$	(8,492)
Other comprehensive income (loss) before reclassifications		364		(478)		(2,616)		(2)
Amounts reclassified from accumulated other comprehensive loss		-		-		-		-
Net current-period other comprehensive income (loss)		364		(478)		(2,616)		(2)
Balance at end of period	\$	(9,634)	\$	(8,494)	\$	(9,634)	\$	(8,494)

Note 10 – Income Taxes

The Company is subject to income tax in multiple jurisdictions and the use of estimates is required to determine the provision for income taxes. For the three months ended June 30, 2020 and 2019, the Company recorded an income tax provision of \$2.5 million and \$4.5 million, respectively. For the six months ended June 30, 2020 and 2019, the Company recorded an income tax provision of \$6.4 million and \$8.7 million, respectively. The income tax provision is based on the estimated annual effective tax rate for the year applied to pre-tax income. The effective income tax rate for the three months ended June 30, 2020 was 16.6 percent compared to 21.9 percent in the same period of the prior year. The effective tax rate decreased by 5.3 percent for the three months ended June 30, 2020 when compared to the same period in 2019 primarily due to an increase in tax benefits from the vesting of restricted stock and the exercise of stock options and an increase in the research and development tax credit. The effective income tax rate for the six months ended June 30, 2020 was 19.4 percent compared to 21.5 percent in the same period of the prior year. The effective tax rate decreased by 2.1 percent for the six months ended June 30, 2020 when compared to the same period in 2019 primarily due to an increase in tax benefits from the vesting of restricted stock and the exercise of stock options and an increase in the research and development tax credit.

The effective income tax rate for the six months ended June 30, 2020 differs from the U.S. federal statutory rate of 21.0 percent due to various factors, including operating in multiple state and foreign jurisdictions and tax credits for which the Company qualifies.

The Company had unrecognized tax benefits totaling \$4.7 million as of June 30, 2020 and \$4.6 million as of December 31, 2019, respectively, all of which, if recognized, would affect the Company's effective tax rate. The Company recognizes interest and penalties related to income tax matters in income tax expense, and reports the liability in current or long-term income taxes payable as appropriate.

The Coronavirus Aid, Relief, and Economic Security (CARES) Act was signed into law on March 27, 2020. The CARES Act is meant to infuse companies with various income and payroll tax cash benefits to ease the impact of the pandemic. A technical correction to the Tax Cuts and Jobs Act of 2017 was included in the CARES Act allowing qualified improvement property to claim bonus depreciation for respective assets placed in service in 2018 and 2019. The impact of the CARES Act to the Company was a \$2.6 million reduction in our income taxes payable and a corresponding increase to our deferred tax liability. In addition, the Company has elected to defer deposits of the employer portion of the Social Security tax for the quarter ended June 30, 2020 through the quarter ended December 31, 2020. The Social Security taxes are being accrued for and will be paid beginning in 2021.

Note 11 – Segment Reporting

The Company's reportable segments are based on the internal reporting used by the Company's Chief Executive Officer, who is the chief operating decision maker (CODM), to assess operating performance and make decisions about the allocation of resources. The Corporate Unallocated and Japan category includes non-reportable segments, as well as research and development and general and administrative costs that the Company does not allocate directly to its operating segments.

Intercompany transactions primarily relate to intercontinental activity and have been eliminated and are excluded from the reported amounts. The difference between income from operations and pre-tax income relates to foreign currency-related gains and losses and interest income on cash balances and investments, which are not allocated to business segments.

Revenue and income from operations by reportable segment for the three and six months ended June 30, 2020 and 2019 were as follows:

(in thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2020	2019	2020	2019
Revenue:				
United States	\$ 86,823	\$ 91,149	\$ 176,899	\$ 178,960
Europe	16,729	20,940	37,516	42,194
Japan	3,023	3,843	7,268	8,230
Total revenue	<u>\$ 106,575</u>	<u>\$ 115,932</u>	<u>\$ 221,683</u>	<u>\$ 229,384</u>

(in thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2020	2019	2020	2019
Income from Operations:				
United States	\$ 24,349	\$ 27,948	\$ 49,438	\$ 54,258
Europe	2,261	3,756	6,625	7,977
Corporate Unallocated and Japan	(12,259)	(12,131)	(24,887)	(23,214)
Total Income from Operations	<u>\$ 14,351</u>	<u>\$ 19,573</u>	<u>\$ 31,176</u>	<u>\$ 39,021</u>

Total long-lived assets at June 30, 2020 and December 31, 2019 were as follows:

(in thousands)	June 30,	December 31,
	2020	2019
Total long-lived assets:		
United States	\$ 220,183	\$ 210,171
Europe	52,817	45,019
Japan	8,129	8,522
Total Assets	<u>\$ 281,129</u>	<u>\$ 263,712</u>

Revenue by product line for the three and six months ended June 30, 2020 and 2019 were as follows:

(in thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2020	2019	2020	2019
Revenue:				
Injection Molding	\$ 57,894	\$ 55,457	\$ 112,670	\$ 110,768
CNC Machining	28,760	38,888	66,645	76,760
3D Printing	14,236	15,266	30,184	29,746
Sheet Metal	4,669	5,472	10,318	10,497
Other Revenue	1,016	849	1,866	1,613
Total revenue	<u>\$ 106,575</u>	<u>\$ 115,932</u>	<u>\$ 221,683</u>	<u>\$ 229,384</u>

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our unaudited consolidated financial statements and related notes appearing elsewhere in this Quarterly Report on Form 10-Q and our Annual Report on Form 10-K for the year ended December 31, 2019.

Forward-Looking Statements

Statements contained in this report regarding matters that are not historical or current facts are “forward-looking statements” within the meaning of The Private Securities Litigation Reform Act of 1995. In some cases, you can identify forward-looking statements by the following words: “may,” “will,” “could,” “would,” “should,” “expect,” “intend,” “plan,” “anticipate,” “believe,” “estimate,” “predict,” “project,” “potential,” “continue,” “ongoing” or the negative of these terms or other comparable terminology, although not all forward-looking statements contain these words. These statements involve known and unknown risks, uncertainties and other factors that may cause our results to be materially different than those expressed or implied in such statements. Certain of these risk factors and others are described in Item 1A. “Risk Factors” of this Form 10-Q, as well as our most recent Annual Report on Form 10-K as filed with the SEC. Other unknown or unpredictable factors also could have material adverse effects on our future results. We cannot guarantee future results, levels of activity, performance or achievements. Accordingly, you should not place undue reliance on these forward-looking statements. Finally, we expressly disclaim any intent or obligation to update any forward-looking statements to reflect subsequent events or circumstances.

Overview

We are the world’s largest and fastest digital manufacturer of custom prototypes and on-demand production parts. We manufacture prototypes and low-volume production parts for companies worldwide, who are under increasing pressure to bring their finished products to market faster than their competition. We utilize injection molding, computer numerical control (CNC) machining, 3D printing and sheet metal fabrication to manufacture custom parts for our customers. Our proprietary technology eliminates most of the time-consuming and expensive skilled labor conventionally required to quote and manufacture parts. Our customers conduct nearly all of their business with us over the Internet. We target our products to the millions of product developers and engineers who use three-dimensional computer-aided design (3D CAD) software to design products across a diverse range of end-markets.

Our primary manufacturing product lines currently include Injection Molding, CNC Machining, 3D Printing and Sheet Metal. We continually seek to expand the range of sizes and geometric complexity of the parts we can make with these processes, to extend the variety of materials we are able to support and to identify additional manufacturing processes to which we can apply our technology in order to better serve the evolving preferences and needs of product developers and engineers.

Injection Molding

Our Injection Molding product line uses our 3D CAD-to-CNC machining technology for the automated design and manufacture of molds, which are then used to produce custom plastic and liquid silicone rubber injection-molded parts and over-molded and insert-molded injection-molded parts on commercially available equipment. Our Injection Molding product line works best for on-demand production, bridge tooling, pilot runs and functional prototyping. Our affordable aluminum molds and quick turnaround times help reduce design risk and limit overall production costs for product developers and engineers. Prototype quantities typically range from 25 to 100 parts. Because we retain possession of the molds, customers who need short-run production often come back to Protolabs’ Injection Molding product line for additional quantities. They do so to support pilot production for product testing, while their tooling for high-volume production is being prepared, because they need on-demand manufacturing due to disruptions in their manufacturing process, because their product requires limited annual quantity or because they need end-of-life production support. In 2017, we launched an on-demand manufacturing injection molding product offering. This product offering utilizes our existing processes, but is designed to fulfill the needs of customers with on-going production needs, typically in annual volumes of less than 10,000 parts.

CNC Machining

Our CNC Machining product line uses commercially available CNC machines to offer milling and turning. CNC milling is a manufacturing process that cuts plastic and metal blocks into one or more custom parts based on the 3D CAD model uploaded by the product developer or engineer. CNC turning with live tooling combines both lathe and mill capabilities to machine parts with cylindrical features from metal rod stock. Our efficiencies derive from the automation of the programming of these machines and a proprietary fixturing process.

Quick-turn CNC machining works best for prototyping, form and fit testing, jigs and fixtures and functional components for end-use applications. The CNC Machining product line is well suited to produce small quantities, typically in the range of one to 1,000 parts.

[Table of Contents](#)

3D Printing

Our 3D Printing product line includes stereolithography, selective laser sintering, direct metal laser sintering, Multi Jet Fusion, PolyJet and digital light synthesis processes, which offer customers a wide-variety of high-quality, precision rapid prototyping and low-volume production. These processes create parts with a high level of accuracy, detail, strength and durability. Industrial 3D Printing is best suited for functional prototypes, complex designs and end-use applications produced in small quantities, typically in the range of one to several hundred parts.

Sheet Metal

Our Sheet Metal product line includes quick-turn and e-commerce-enabled custom sheet metal parts, which provides customers with prototype and low-volume production parts. The rapid prototype sheet metal process is most often used when form, fit and function are all a priority. Our manufacturing process uses customer 3D CAD models uploaded by the product developer or engineer to fabricate quick-turn prototype sheet metal or short-run production parts. The Sheet Metal product line is well suited to produce quantities in the range of one to 500 parts.

Key Financial Measures and Trends

Revenue

Our operations are comprised of three geographic operating segments in the United States, Europe and Japan. Revenue is derived from our Injection Molding, CNC Machining, 3D Printing and Sheet Metal product lines. Injection Molding revenue consists of sales of custom injection molds and injection-molded parts. CNC Machining revenue consists of sales of CNC-machined custom parts. 3D Printing revenue consists of sales of 3D-printed parts. Sheet Metal revenue consists of sales of fabricated sheet metal custom parts. Our historical and current efforts to increase revenue have been directed at expanding the breadth of our product offerings, gaining new customers and selling to our existing customer base by increasing marketing and selling activities, including:

- expanding the breadth and scope of each of our product lines by adding more sizes and materials to our offerings;
- the introduction of our 3D Printing product line through our acquisition of FineLine in 2014;
- expanding 3D Printing to Europe through our acquisition of Alphaform in October 2015;
- the introduction of our Sheet Metal product line through our acquisition of Rapid Manufacturing Group, LLC (RAPID) in 2017; and
- continuously improving the usability of our product lines such as our web-centric applications.

During the three months ended June 30, 2020, we served 17,037 unique product developers and engineers who purchase our products through our web-based customer interface, a decrease of 18.2% over the same period in 2019. During the six months ended June 30, 2020, we served 29,703 unique product developers and engineers who purchase our products through our web-based customer interface, a decrease of 5.9% over the same period in 2019. The economic uncertainty arising from the COVID-19 pandemic has impacted the number of product developers and engineers who purchase our products. While we expect the number of product developers and engineers served to grow in the long-term, challenges posed by the COVID-19 pandemic on the global economy have continued through the date of this report. Steps taken by national and local governments to slow the spread of the virus, including business shutdowns and shelter in place orders, have hindered the ability and willingness of project developers and engineers to proceed with development and commercialization projects on the same scale as they have historically. At this time, it is difficult to predict the future given the current economic uncertainty and evolving market conditions.

Cost of Revenue, Gross Profit and Gross Margin

Cost of revenue consists primarily of raw materials, equipment depreciation, employee compensation, benefits, stock-based compensation, facilities costs and overhead allocations associated with the manufacturing process for molds and custom parts. We expect our personnel-related costs to increase in order to retain and attract top talent and remain competitive in the market. Overall, we expect cost of revenue to increase in absolute dollars, but remain relatively constant as a percentage of total revenue.

We define gross profit as our revenue less our cost of revenue, and we define gross margin as gross profit expressed as a percentage of revenue. Our gross profit and gross margin are affected by many factors, including our mix of revenue by product line, pricing, sales volume, manufacturing costs, the costs associated with increasing production capacity, the mix between domestic and foreign revenue sources and foreign exchange rates.

[Table of Contents](#)

Operating Expenses

Operating expenses consist of marketing and sales, research and development and general and administrative expenses. Personnel-related costs are the most significant component in each of these categories.

Our recent decrease in operating expenses is mainly due to cost saving measures implemented as a result of the COVID-19 pandemic. However, our long-term business strategy is to continue to be a leading online and technology-enabled manufacturer of quick-turn, on-demand injection-molded, CNC-machined, CNC-turned, 3D-printed and sheet metal custom parts for prototyping and low-volume production. In order to achieve our long-term goals and support our revenue growth, we anticipate continued substantial investments in technology and personnel, resulting in increased operating expenses.

Marketing and sales. Marketing and sales expense consists primarily of employee compensation, benefits, commissions, stock-based compensation, marketing programs such as electronic, print and pay-per-click advertising, trade shows and other related overhead. We expect sales and marketing expense to increase in the future as we increase the number of marketing and sales professionals and marketing programs targeted to increase our customer base and grow revenue.

Research and development. Research and development expense consists primarily of personnel and outside service costs related to the development of new processes and product lines, enhancement of existing product lines, development of software for internal use, maintenance of internally developed software, quality assurance and testing. Costs for internal use software are evaluated by project and capitalized where appropriate under ASC 350-40, *Intangibles — Goodwill and Other, Internal-Use Software*. We expect research and development expense to increase in the future as we seek to enhance our e-commerce interface technology, internal software and supporting business systems, and continue to expand our product lines.

General and administrative. General and administrative expense consists primarily of employee compensation, benefits, stock-based compensation, professional service fees related to accounting, tax and legal and other related overhead. We expect general and administrative expense to increase in the future as we continue to grow and expand as a global organization.

Other Income, net

Other income, net primarily consists of foreign currency-related gains and losses and interest income on cash balances and investments. Our foreign currency-related gains and losses will vary depending upon movements in underlying exchange rates. Our interest income will vary each reporting period depending on our average cash balances during the period, composition of our marketable security portfolio and the current level of interest rates.

Provision for Income Taxes

Provision for income taxes is comprised of federal, state, local and foreign taxes based on pre-tax income. Overall, we expect our effective tax rate for 2020 and beyond will remain consistent based on the current tax laws.

Market Conditions

On March 11, 2020, the World Health Organization declared the outbreak of the novel coronavirus (COVID-19) a pandemic. The full financial impact of COVID-19 is unknown at this time and will depend on the duration of government restrictions, including travel restrictions, quarantines, shelter in place orders and shutdowns and duration of the economic slowdown and nature and timing of a recovery. The Company has been deemed an essential business and all of our global manufacturing operations have remained open. The Company has activated a global, cross-functional response team, which is closely monitoring the situation and implementing additional safety measures to help ensure the well-being of our employees, customers and suppliers, to minimize disruptions and provide for the safe and reliable supply of products to our customers. In accordance with the guidance provided by both the World Health Organization and the U.S. Centers for Disease Control and Prevention, the Company has implemented safe work practices, including social distancing and work from home guidelines.

We are actively monitoring key product availability and continue to stay connected with our customers to understand impacts on their operations. All of these efforts will help us better plan and prepare, so we can continue to be a leading supplier of custom parts. In anticipation of exposure due to an economic slowdown driven by COVID-19, the Company increased its bad debt reserve by \$0.9 million as of June 30, 2020.

The Coronavirus Aid, Relief, and Economic Security (CARES) Act was signed into law on March 27, 2020. The CARES Act is meant to infuse companies with various income and payroll tax cash benefits to ease the impact of the pandemic. A technical correction to the Tax Cuts and Jobs Act of 2017 was included in the CARES Act allowing qualified improvement property to claim bonus depreciation for respective assets placed in service in 2018 and 2019. The impact of the CARES Act to the Company was a \$2.6 million reduction in our income taxes payable and a corresponding increase to our deferred tax liability. In addition, the Company has elected to defer deposits of the employer portion of the Social Security tax for the quarter ended June 30, 2020 through the quarter ended December 31, 2020. The Social Security taxes are being accrued for and will be paid beginning in 2021.

See "Risk Factors" in Item 1A of this Quarterly Report on Form 10-Q for further information of the possible impact of the COVID-19 pandemic on our business.

[Table of Contents](#)

Results of Operations

The following table summarizes our results of operations and the related changes for the periods indicated. The results below are not necessarily indicative of the results for future periods.

(dollars in thousands)	Three Months Ended June 30,				Change		Six Months Ended June 30,				Change	
	2020		2019		\$	%	2020		2019		\$	%
Revenue	\$ 106,575	100.0	\$ 115,932	100.0	\$ (9,357)	(8.1)	\$ 221,683	100.0	\$ 229,384	100.0	\$ (7,701)	(3.4)
Cost of revenue	54,119	50.8	55,696	48.0	(1,577)	(2.8)	111,127	50.1	110,288	48.1	839	0.8
Gross profit	52,456	49.2	60,236	52.0	(7,780)	(12.9)	110,556	49.9	119,096	51.9	(8,540)	(7.2)
Operating expenses:												
Marketing and sales	16,936	15.9	19,285	16.6	(2,349)	(12.2)	35,116	15.8	37,862	16.5	(2,746)	(7.3)
Research and development	8,648	8.1	8,169	7.1	479	5.9	17,635	8.0	16,182	7.1	1,453	9.0
General and administrative	12,521	11.7	13,209	11.4	(688)	(5.2)	26,629	12.0	26,031	11.3	598	2.3
Total operating expenses	38,105	35.8	40,663	35.1	(2,558)	(6.3)	79,380	35.8	80,075	34.9	(695)	(0.9)
Income from operations	14,351	13.5	19,573	16.9	(5,222)	(26.7)	31,176	14.1	39,021	17.0	(7,845)	(20.1)
Other income, net	767	0.7	1,125	1.0	(358)	(31.8)	1,821	0.8	1,338	0.6	483	36.1
Income before income taxes	15,118	14.2	20,698	17.9	(5,580)	(27.0)	32,997	14.9	40,359	17.6	(7,362)	(18.2)
Provision for income taxes	2,511	2.4	4,532	3.9	(2,021)	(44.6)	6,406	2.9	8,682	3.8	(2,276)	(26.2)
Net income	\$ 12,607	11.8%	\$ 16,166	14.0%	\$ (3,559)	(22.0)%	\$ 26,591	12.0%	\$ 31,677	13.8%	\$ (5,086)	(16.1)%

Stock-based compensation expense included in the statements of operations data above for the three and six months ended June 30, 2020 and 2019 was as follows:

(dollars in thousands)	Three Months Ended June 30,		Six Months Ended June 30,	
	2020	2019	2020	2019
Stock options and restricted stock	\$ 3,331	\$ 3,193	\$ 6,069	\$ 5,972
Employee stock purchase plan	308	293	603	554

Total stock-based compensation expense	\$ 3,639	\$ 3,486	\$ 6,672	\$ 6,526
Cost of revenue	\$ 594	\$ 485	\$ 1,115	\$ 906
Operating expenses:				
Marketing and sales	750	614	1,368	1,163
Research and development	607	503	1,128	926
General and administrative	1,688	1,884	3,061	3,531
Total stock-based compensation expense	\$ 3,639	\$ 3,486	\$ 6,672	\$ 6,526

[Table of Contents](#)
Comparison of Three Months Ended June 30, 2020 and 2019
Revenue

Revenue by reportable segment and the related changes for the three months ended June 30, 2020 and 2019 were as follows:

(dollars in thousands)	Three Months Ended June 30,				Change	
	2020		2019		\$	%
	\$	% of Total Revenue	\$	% of Total Revenue		
Revenue						
United States	\$ 86,823	81.5%	\$ 91,149	78.6%	\$ (4,326)	(4.7)%
Europe	16,729	15.7	20,940	18.1	(4,211)	(20.1)
Japan	3,023	2.8	3,843	3.3	(820)	(21.3)
Total revenue	\$ 106,575	100.0%	\$ 115,932	100.0%	\$ (9,357)	(8.1)%

Our revenue decreased \$9.4 million, or 8.1%, for the three months ended June 30, 2020 compared to the same period in 2019. By reportable segment, revenue in the United States decreased \$4.3 million, or 4.7%, for the three months ended June 30, 2020 compared to the same period in 2019. Revenue in Europe decreased \$4.2 million, or 20.1%, and revenue in Japan decreased \$0.8 million, or 21.3%, in each case for the three months ended June 30, 2020 compared to the same period in 2019. Our revenue in Europe was impacted by foreign currency exchange rates. Excluding the \$0.4 million impact of the changes in foreign currency exchange rates, the decrease in Europe revenue would have been 18.1%. In addition, our revenue in each region was impacted by a decline in order activity driven by current economic conditions as a result of the COVID-19 pandemic.

Our revenue decline during the three months ended June 30, 2020 was the result of a decrease in the volume of product developers and engineers we served. During the three months ended June 30, 2020, we served 17,037 unique product developers and engineers, a decrease of 18.2% over the same period in 2019. The economic uncertainty arising from the COVID-19 pandemic has impacted the number of product developers and engineers who purchase our products. While we expect the number of product developers and engineers served to grow in the long-term, challenges posed by the COVID-19 pandemic on the global economy have continued through the date of this report. Steps taken by national and local governments to slow the spread of the virus, including business shutdowns and shelter in place orders, have hindered the ability and willingness of project developers and engineers to proceed with development and commercialization projects on the same scale as they have historically. At this time, it is difficult to predict the future given the current economic uncertainty and evolving market conditions.

Our revenue decreases were primarily driven by a decline in order activity as a result of the economic uncertainty created by the COVID-19 pandemic. International revenue was negatively impacted by \$0.4 million during the three months ended June 30, 2020 compared to the same period in 2019 as a result of foreign currency movements, primarily the weakening of the British Pound and Euro relative to the United States Dollar.

Revenue by product line and the related changes for the three months ended June 30, 2020 and 2019 were as follows:

(dollars in thousands)	Three Months Ended June 30,				Change	
	2020		2019		\$	%
	\$	% of Total Revenue	\$	% of Total Revenue		
Revenue						
Injection Molding	\$ 57,894	54.3%	\$ 55,457	47.8%	\$ 2,437	4.4%
CNC Machining	28,760	27.0	38,888	33.5	(10,128)	(26.0)
3D Printing	14,236	13.3	15,266	13.2	(1,030)	(6.7)
Sheet Metal	4,669	4.4	5,472	4.7	(803)	(14.7)
Other Revenue	1,016	1.0	849	0.8	167	19.7
Total revenue	\$ 106,575	100.0%	\$ 115,932	100.0%	\$ (9,357)	(8.1)%

By product line, our revenue decrease was driven by a 26.0% decrease in CNC Machining revenue, a 6.7% decrease in 3D Printing revenue, and a 14.7% decrease in Sheet Metal revenue, which was partially offset by a 4.4% increase in Injection Molding revenue and a 19.7% increase in Other Revenue, in each case for the three months ended June 30, 2020 compared to the same period in 2019.

[Table of Contents](#)

Cost of Revenue, Gross Profit and Gross Margin

Cost of Revenue. Cost of revenue decreased \$1.6 million, or 2.8%, for the three months ended June 30, 2020 compared to the same period in 2019, which was less than the rate of revenue decrease of 8.1% for the three months ended June 30, 2020 compared to the same period in 2019. The decrease in cost of revenue was primarily driven by lower revenue volumes and cost saving measures implemented as a result of the COVID-19 pandemic. Specifically, the decreases were driven by a decrease in direct labor headcount and hours worked resulting in personnel and related cost decreases of \$1.5 million and raw material and production cost decreases of \$0.6 million, which were partially offset by equipment and facility-related cost increases of \$0.5 million to support future growth of the business.

Gross Profit and Gross Margin. Gross profit decreased from \$60.2 million in the three months ended June 30, 2019 to \$52.5 million in the three months ended June 30, 2020. Gross margin decreased from 52.0% in the three months ended June 30, 2019 to 49.2% in the three months ended June 30, 2020 primarily due to the fixed cost structure of our facilities and equipment supporting lower revenue this quarter and the timing and mix of revenue.

Operating Expenses, Other Income, net and Provision for Income Taxes

Marketing and Sales. Marketing and sales expenses decreased \$2.3 million, or 12.2%, during the three months ended June 30, 2020 compared to the same period in 2019 due primarily to personnel and related cost decreases of \$1.0 million as well as marketing program cost decreases of \$1.3 million.

Research and Development. Our research and development expenses increased \$0.5 million, or 5.9%, during the three months ended June 30, 2020 compared to the same period in 2019 due to an increase in headcount resulting in personnel and related cost increases of \$0.5 million.

General and Administrative. Our general and administrative expenses decreased \$0.7 million, or 5.2%, during the three months ended June 30, 2020 compared to the same period in 2019 due to administrative cost decreases of \$0.5 million, amortization cost decreases of \$0.1 million and stock-based compensation cost decreases of \$0.2 million, which were partially offset by professional service cost increases of \$0.1 million.

Other Income, net. We recognized other income, net of \$0.8 million for the three months ended June 30, 2020, a decrease of \$0.4 million compared to other income, net of \$1.1 million for the three months ended June 30, 2019. Other income, net for the three months ended June 30, 2020 primarily consisted of \$0.4 million in interest income on investments and a \$0.3 million gain on foreign currency. Other income, net for the three months ended June 30, 2019 primarily consisted of \$0.5 million in interest income on investments and a \$0.5 million gain on foreign currency.

Provision for Income Taxes. Our effective tax rate of 16.6% for the three months ended June 30, 2020 decreased 5.3% compared to 21.9% for the same period in 2019. The decrease in the effective tax rate is primarily due to an increase in tax benefits from the vesting of restricted stock and the exercise of stock options and an increase in the research and development tax credit. Our income tax provision of \$2.5 million for the three months ended June 30, 2020 decreased \$2.0 million compared to our income tax provision of \$4.5 million for the three months ended June 30, 2019.

[Table of Contents](#)

Comparison of Six Months Ended June 30, 2020 and 2019

Revenue

Revenue by reportable segment and the related changes for the six months ended June 30, 2020 and 2019 were as follows:

(dollars in thousands)	Six Months Ended June 30,				Change	
	2020		2019			
	\$	% of Total Revenue	\$	% of Total Revenue	\$	%
Revenue						
United States	\$ 176,899	79.8%	\$ 178,960	78.0%	\$ (2,061)	(1.2)%
Europe	37,516	16.9	42,194	18.4	(4,678)	(11.1)
Japan	7,268	3.3	8,230	3.6	(962)	(11.7)
Total revenue	\$ 221,683	100.0%	\$ 229,384	100.0%	\$ (7,701)	(3.4)%

Our revenue decreased \$7.7 million, or 3.4%, for the six months ended June 30, 2020 compared to the same period in 2019. By reportable segment, revenue in the United States decreased \$2.1 million, or 1.2%, for the six months ended June 30, 2020 compared to the same period in 2019. Revenue in Europe decreased \$4.7 million, or 11.1%, and revenue in Japan decreased \$1.0 million, or 11.7%, in each case for the six months ended June 30, 2020 compared to the same period in 2019. Our revenue in Europe was impacted by foreign currency exchange rates. Excluding the \$1.1 million impact of the changes in foreign currency exchange rates, the decrease in Europe revenue would have been 8.6%. In addition, our revenue in each region was impacted by a decline in order activity driven by current economic conditions as a result of the COVID-19 pandemic.

Our revenue decline during the six months ended June 30, 2020 was the result of a decrease in the volume of product developers and engineers we served. During the six months ended June 30, 2020, we served 29,703 unique product developers and engineers, a decrease of 5.9% over the same period in 2019. The economic uncertainty arising from the COVID-19 pandemic has impacted the number of product developers and engineers who purchase our products. While we expect the number of product developers and engineers served to grow in the long-term, challenges posed by the COVID-19 pandemic on the global economy have continued through the date of this report. Steps taken by national and local governments to slow the spread of the virus, including business shutdowns and shelter in place orders, have hindered the ability and willingness of project developers and engineers to proceed with development and commercialization projects on the same scale as they have historically. At this time, it is difficult to predict the future given the current economic uncertainty and evolving market conditions.

Our revenue decreases were primarily driven by a decline in order activity as a result of the economic uncertainty created by the COVID-19 pandemic. International revenue was negatively impacted by \$0.9 million during the six months ended June 30, 2020 compared to the same period in 2019 as a result of foreign currency movements, primarily the weakening of the British Pound and Euro relative to the United States Dollar.

Revenue by product line and the related changes for the six months ended June 30, 2020 and 2019 were as follows:

(dollars in thousands)	Six Months Ended June 30,				Change	
	2020		2019		\$	%
	\$	% of Total Revenue	\$	% of Total Revenue		
Revenue						
Injection Molding	\$ 112,670	50.8%	\$ 110,768	48.3%	\$ 1,902	1.7%
CNC Machining	66,645	30.1	76,760	33.5	(10,115)	(13.2)
3D Printing	30,184	13.6	29,746	13.0	438	1.5
Sheet Metal	10,318	4.7	10,497	4.6	(179)	(1.7)
Other Revenue	1,866	0.8	1,613	0.6	253	15.7
Total revenue	\$ 221,683	100.0%	\$ 229,384	100.0%	\$ (7,701)	(3.4)%

By product line, our revenue decrease was driven by a 13.2% decrease in CNC Machining revenue and a 1.7% decrease in Sheet Metal revenue, which was partially offset by a 1.7% increase in Injection Molding revenue, a 1.5% increase in 3D Printing revenue and a 15.7% increase in Other Revenue, in each case for the six months ended June 30, 2020 compared to the same period in 2019.

[Table of Contents](#)

Cost of Revenue, Gross Profit and Gross Margin

Cost of Revenue. Cost of revenue increased \$0.8 million, or 0.8%, for the six months ended June 30, 2020 compared to the same period in 2019, despite the rate of revenue decrease of 3.4% for the six months ended June 30, 2020 compared to the same period in 2019. The increases were driven by a \$1.6 million increase in equipment and facility-related costs to support future growth of the business, which was partially offset by personnel and related cost decreases of \$0.8 million.

Gross Profit and Gross Margin. Gross profit decreased from \$119.1 million in the six months ended June 30, 2019 to \$110.6 million in the six months ended June 30, 2020 primarily due to a decrease in revenue. Gross margin decreased from 51.9% in the six months ended June 30, 2019 to 49.9% in the six months ended June 30, 2020 due to the fixed cost structure of our facilities and equipment supporting lower revenue this year and the timing and mix of revenue.

Operating Expenses, Other Income, net and Provision for Income Taxes

Marketing and Sales. Marketing and sales expenses decreased \$2.7 million, or 7.3%, during the six months ended June 30, 2020 compared to the same period in 2019 due primarily to personnel and related cost decreases of \$1.2 million as well as marketing program cost decreases of \$1.5 million.

Research and Development. Our research and development expenses increased \$1.5 million, or 9.0%, during the six months ended June 30, 2020 compared to the same period in 2019 due to an increase in headcount resulting in personnel and related cost increases of \$1.4 million and operating cost increases of \$0.1 million.

General and Administrative. Our general and administrative expenses increased \$0.6 million, or 2.3%, during the six months ended June 30, 2020 compared to the same period in 2019 due to personnel and related cost increases of \$1.2 million and professional services increases of \$0.2 million, which were partially offset by stock-based compensation decreases of \$0.5 million, as well as a \$0.3 million decrease in amortization cost.

Other Income, net. We recognized other income, net of \$1.8 million for the six months ended June 30, 2020, an increase of \$0.5 million compared to other income, net of \$1.3 million for the six months ended June 30, 2019. Other income, net for the six months ended June 30, 2020 primarily consisted of \$0.9 million in interest income on investments and a \$0.9 million gain on foreign currency. Other income, net for the six months ended June 30, 2019 primarily consisted of \$1.1 million in interest income on investments and a \$0.1 million gain on foreign currency.

Provision for Income Taxes. Our effective tax rate of 19.4% for the six months ended June 30, 2020 decreased 2.1% compared to 21.5% for the same period in 2019. The decrease in the effective tax rate is primarily due to an increase in tax benefits from the vesting of restricted stock and the exercise of stock options and an increase in the research and development tax credit. Our income tax provision of \$6.4 million for the six months ended June 30, 2020 decreased \$2.3 million compared to our income tax provision of \$8.7 million for the six months ended June 30, 2019.

Liquidity and Capital Resources*Cash Flows*

The following table summarizes our cash flows during the six months ended June 30, 2020 and 2019:

(dollars in thousands)	Six Months Ended June 30,	
	2020	2019
Net cash provided by operating activities	\$ 53,417	\$ 54,888
Net cash used in investing activities	(65,292)	(17,949)
Net cash used in financing activities	(15,198)	(21,585)
Effect of exchange rates on cash and cash equivalents	(149)	135
Net (decrease) increase in cash and cash equivalents	<u>\$ (27,222)</u>	<u>\$ 15,489</u>

Sources of Liquidity

Historically, we have primarily financed our operations and capital expenditures through cash flow from operations. We had cash and cash equivalents of \$98.0 million as of June 30, 2020, a decrease of \$27.2 million from December 31, 2019. The decrease in our cash was primarily due to cash used in investing activity including net investments in marketable securities of \$29.0 million and purchases of property, equipment and other capital assets of \$33.3 million and repurchases of common stock of \$14.7 million, which were partially offset by cash generated through operations of \$53.4 million.

Cash Flows from Operating Activities

Cash flows from operating activities were \$53.4 million during the six months ended June 30, 2020 and primarily consisted of net income of \$26.6 million, adjusted for certain non-cash items, including depreciation and amortization of \$15.9 million, stock-based compensation expense of \$6.7 million and deferred taxes of \$5.7 million, which were partially offset by changes in operating assets and liabilities and other items totaling \$1.5 million. Cash flows from operating activities were \$54.9 million during the six months ended June 30, 2019 and primarily consisted of net income of \$31.7 million, adjusted for certain non-cash items, including depreciation and amortization of \$15.0 million, stock-based compensation expense of \$6.5 million, deferred taxes of \$1.6 million and changes in operating assets and liabilities and other items totaling \$0.1 million.

Cash flows from operating activities decreased \$1.5 million during the six months ended June 30, 2020 compared to the same period in 2019, primarily due to decreases in net income of \$5.1 million, decreases in changes in operating assets and liabilities of \$1.0 million driven by timing of cash receipts and payments, and decreases of \$0.4 million in other items, which were partially offset by increases in deferred taxes of \$4.1 million and increases in depreciation and amortization of \$0.9 million.

Cash Flows from Investing Activities

Cash used in investing activities was \$65.3 million during the six months ended June 30, 2020, consisting of \$29.0 million in net investments in marketable securities, \$33.3 million for the purchases of property, equipment and other capital assets and \$3.0 million for purchases of other assets and investments.

Cash used in investing activities was \$17.9 million during the six months ended June 30, 2019, consisting of \$34.1 million for the purchases of property, equipment and other capital assets, \$9.0 million for purchases of marketable securities and \$4.0 million for purchases of other assets and investments, which were partially offset by \$29.2 million in proceeds from maturities of marketable securities.

Cash Flows from Financing Activities

Cash used in financing activities was \$15.2 million during the six months ended June 30, 2020, consisting of \$14.7 million in repurchases of common stock and \$3.4 million in purchases of shares withheld for tax obligations associated with equity transactions, which were partially offset by \$2.9 million in proceeds from the exercise of stock options.

Cash used in financing activities was \$21.6 million during the six months ended June 30, 2019, consisting of \$21.4 million in repurchases of common stock and \$2.4 million in purchases of shares withheld for tax obligations associated with equity transactions, which were partially offset by \$2.2 million in proceeds from the exercise of stock options.

Off-Balance Sheet Arrangements

Since our inception, we have not engaged in any off-balance sheet arrangements, including the use of structured finance, special purpose entities or variable interest entities.

Critical Accounting Policies and Use of Estimates

We have adopted various accounting policies to prepare the Consolidated Financial Statements in accordance with accounting principles generally accepted in the United States of America (U.S. GAAP). Our significant accounting policies are disclosed in Note 2 to the Consolidated Financial Statements included in our Annual Report on Form 10-K for the year ended December 31, 2019.

Recent Accounting Pronouncements

For information on recent accounting pronouncements, see Note 2 to the Consolidated Financial Statements appearing in Part I, Item 1 in this Quarterly Report on Form 10-Q.

25

[Table of Contents](#)

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Foreign Currency Risk

As a result of our foreign operations, we have revenue, expenses, assets and liabilities that are denominated in foreign currencies. We generate revenue and incur production costs and operating expenses in British Pounds, Euros and Japanese Yen.

Our operating results and cash flows are adversely impacted when the United States Dollar appreciates relative to foreign currencies. Additionally, our operating results and cash flows are adversely impacted when the British Pound appreciates relative to the Euro. As we expand internationally, our results of operations and cash flows will become increasingly subject to changes in foreign currency exchange rates.

We have not used forward contracts or currency borrowings to hedge our exposure to foreign currency risk. Foreign currency risk can be assessed by estimating the change in results of operations or financial position resulting from a hypothetical 10% adverse change in foreign exchange rates. We believe such a change would generally not have a material impact on our financial position, but could have a material impact on our results of operations. We recognized foreign currency gains of \$0.3 million and \$0.9 million during the three and six months ended June 30, 2020, respectively. We recognized foreign currency gains of \$0.5 million and \$0.1 million during the three and six months ended June 30, 2019, respectively. The changes in foreign exchange rates had a negative impact on consolidated revenue of \$0.4 million for the three months ended June 30, 2020 and \$0.9 million for the six months ended June 30, 2020 as compared to the same periods in 2019.

26

[Table of Contents](#)

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as defined in Rule 13a-15(e) under the Securities Exchange Act of 1934 (Exchange Act)) as of the end of the period covered by this report. Based upon that evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of the period covered by this quarterly report, our disclosure controls and procedures are effective and provide reasonable assurance that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported accurately and within the time frames specified in the SEC's rules and forms and accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There have been no changes in our internal control over financial reporting (as such term is defined in Rule 13a-15(f) under the Exchange Act) during the period covered by this report that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

27

[Table of Contents](#)

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

From time to time, we are subject to various legal proceedings and claims that arise in the ordinary course of our business activities. Although the results of litigation and claims cannot be predicted with certainty, as of the date of these financial statements, we do not believe we are party to any litigation the outcome of which, if determined adversely to us, would individually or in the aggregate be reasonably expected to have a material adverse effect on our business.

Item 1A. Risk Factors

Part I, Item 1A. "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2019 includes a discussion of our risk factors. The information presented below updates, and should be read in conjunction with, the risk factors and information disclosed in our Form 10-K. Except as presented below, there have been no material changes from the risk factors described in our Form 10-K.

Economic uncertainty arising from the recent COVID-19 pandemic could adversely affect our business and results of operations.

On March 11, 2020, the World Health Organization declared the outbreak of the novel coronavirus (COVID-19) a pandemic. The COVID-19 outbreak and associated counter-acting measures implemented by governments around the world, as well as increased business uncertainty, could adversely affect our business and results of operations. At this time, the Company is monitoring the global outbreak of the COVID-19 and is taking steps to mitigate the risks to our employees, customers, suppliers and other stakeholders. The Company has been deemed an essential business and all of our global manufacturing operations have remained open. The current business environment and quickly evolving market conditions require significant management judgment to interpret and quantify the potential impact on our assumptions about future financial performance and operating cash flows. To the extent that changes in

the current business environment impact our ability to achieve levels of forecasted operating results and cash flows, if our stock price were to trade below book value per share for an extended period of time and/or should other events occur indicating the carrying value of our assets might be impaired, we may be required to recognize impairment losses on goodwill, intangible and tangible assets.

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

On February 9, 2017, we announced that our board of directors had authorized the repurchase of shares of our common stock from time to time on the open market or in privately negotiated purchases, at an aggregate purchase price of up to \$50 million. On May 16, 2019, we announced that our board of directors approved a \$50 million increase in its authorized stock repurchase program and extended the term of the program through December 31, 2023. This authorization increases the stock repurchase program to \$100 million.

The timing and amount of any share repurchases will be determined by our management based on market conditions and other factors.

The common stock repurchase does not obligate us to repurchase any dollar amount or number of shares. During the three months ended June 30, 2020, we repurchased 38,154 shares of our common stock at a total purchase price of \$2.7 million under this program. Common stock repurchase activity through June 30, 2020 was as follows:

Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs (in thousands) (1)
April 1, 2020 through April 30, 2020	38,154	\$ 70.81	38,154	\$ 35,175
May 1, 2020 through May 31, 2020	-	\$ -	-	\$ 35,175
June 1, 2020 through June 30, 2020	-	\$ -	-	\$ 35,175
	<u>38,154</u>	<u>\$ 70.81</u>	<u>38,154</u>	<u>\$ 35,175</u>

(1) Effective May 15, 2019 the Board of Directors authorized the repurchase of shares of the Company's common stock from time to time on the open market or in privately negotiated purchases, at an aggregate purchase price of up to \$100 million. The term of the program runs through December 31, 2023.

Item 3. Defaults Upon Senior Securities

No matters to disclose.

Item 4. Mine Safety Disclosures

No matters to disclose.

Item 5. Other Information

No matters to disclose.

[Table of Contents](#)

Item 6. Exhibits

The following documents are filed as part of this report:

Exhibit Number	Description of Exhibit
3.1 ⁽¹⁾	Third Amended and Restated Articles of Incorporation of Proto Labs, Inc.
3.2 ⁽²⁾	Articles of Amendment to Third Amended and Restated Articles of Incorporation of Proto Labs, Inc. dated May 20, 2015
3.3 ⁽³⁾	Second Amended and Restated By-Laws of Proto Labs, Inc., as amended through November 8, 2016
31.1	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act
31.2	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act
32.1	Certification of the Chief Executive Officer and the Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act
101.INS	Inline XBRL Instance Document (the Instance Document does not appear in the Interactive Data File because its XBRL tags are embedded within the Inline XBRL document)
101.SCH	Inline XBRL Taxonomy Extension Schema Document
101.CAL	Inline XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF	Inline XBRL Taxonomy Extension Definition Linkbase Document
101.LAB	Inline XBRL Taxonomy Extension Label Linkbase Document
101.PRE	Inline XBRL Taxonomy Extension Presentation Linkbase Document
104	Cover Page Interactive Data File (formatted as Inline XBRL and contained in Exhibit 101)

(1) Previously filed as Exhibit 3.2 to the Company's Registration Statement on Form S-1/A (File No. 333-175745), filed with the Commission on February 13, 2012, and incorporated by reference herein.

(2)

Previously filed as Exhibit 3.1 to the Company's Form 8-K (File No. 001-35435), filed with the Commission on May 21, 2015 and incorporated by reference herein.

- (3) Previously filed as Exhibit 3.1 to the Company's Form 8-K (File No. 001-35435), filed with the Commission on November 8, 2016 and incorporated by reference herein.

[Table of Contents](#)

SIGNATURE

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.

Proto Labs, Inc.

Date: July 31, 2020

/s/ Victoria M. Holt

Victoria M. Holt
President and Chief Executive Officer
(Principal Executive Officer)

Date: July 31, 2020

/s/ John A. Way

John A. Way
Chief Financial Officer
(Principal Financial Officer)

**CERTIFICATION PURSUANT TO RULE 13a-14(a) OR 15d-14(a) OF
THE SECURITIES EXCHANGE ACT OF 1934,
AS ADOPTED PURSUANT TO SECTION 302 OF
THE SARBANES-OXLEY ACT OF 2002**

I, Victoria M. Holt, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Proto Labs, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
 - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: July 31, 2020

By: /s/ Victoria M. Holt
Victoria M. Holt
President and Chief Executive Officer
(Principal Executive Officer)

**CERTIFICATION PURSUANT TO RULE 13a-14(a) OR 15d-14(a) OF
THE SECURITIES EXCHANGE ACT OF 1934,
AS ADOPTED PURSUANT TO SECTION 302 OF
THE SARBANES-OXLEY ACT OF 2002**

I, John A. Way, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Proto Labs, Inc.;

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

- a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
- b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
- c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
- d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

- a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
- b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: July 31, 2020

By: /s/ John A. Way

John A. Way
Chief Financial Officer
(Principal Financial Officer)

**CERTIFICATION OF CHIEF EXECUTIVE OFFICER AND CHIEF FINANCIAL OFFICER
PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

I, Victoria M. Holt, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report of Proto Labs, Inc. on Form 10-Q for the fiscal quarter ended June 30, 2020 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Quarterly Report on Form 10-Q fairly presents in all material respects the financial condition and results of operations of Proto Labs, Inc.

Date: July 31, 2020

By: /s/ Victoria M. Holt
Name: Victoria M. Holt
Title: President and Chief Executive Officer

I, John A. Way, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that the Quarterly Report of Proto Labs, Inc. on Form 10-Q for the fiscal quarter ended June 30, 2020 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 and that information contained in such Quarterly Report on Form 10-Q fairly presents in all material respects the financial condition and results of operations of Proto Labs, Inc.

Date: July 31, 2020

By: /s/ John A. Way
Name: John A. Way
Title: Chief Financial Officer
