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, 2013

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)

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 and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). ☒ Yes ☐ No

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

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date: 25,335,456 shares of Common Stock, par value $0.001 per share, were outstanding at July 31, 2013.

Proto Labs, Inc.
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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

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

	June 30, 2013 (Unaudited)	December 31, 2012
Assets		
Current assets		
Cash and cash equivalents	$ 35,446	$ 36,759
Short-term marketable securities	30,330	25,137
Accounts receivable, net of allowance for doubtful accounts of $158 and $154 as of June 30, 2013 and December 31, 2012, respectively	17,529	15,791
Inventory	4,875	4,619
Prepaid expenses and other current assets	3,454	5,364
Income taxes receivable	4,720	1,877
Deferred tax assets	287	609
Total current assets	96,641	90,156
Property and equipment, net	47,144	45,316
Long-term marketable securities	54,169	36,965
Other assets	246	285
Total assets	$ 198,200	$ 172,722
Liabilities and shareholders’ equity		
Current liabilities		
Accounts payable	$ 5,712	$ 4,758
Accrued compensation	4,372	5,995
Accrued liabilities and other	623	513
Current portion of long-term debt obligations	180	273
Total current liabilities	10,887	11,539
Long-term deferred tax liabilities	3,346	3,346
Long-term debt obligations	241	356
Other long-term liabilities	700	782
Total liabilities	15,174	16,023
Shareholders’ equity		
Preferred stock, $0.001 par value, authorized 10,000,000 shares; issued and outstanding 0 shares as of June 30, 2013 and December 31, 2012, respectively	—	—
Common stock, $0.001 par value, authorized 150,000,000 shares; issued and outstanding 25,304,743 and 24,803,640 shares as of June 30, 2013 and December 31, 2012, respectively	26	25
Additional paid in capital	157,565	147,032
Retained earnings	27,468	10,570
Accumulated other comprehensive income (loss)	(2,033)	(928)
Total shareholders’ equity	183,026	156,699
Total liabilities and shareholders’ equity	$ 198,200	$ 172,722

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

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

	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Statements of Operations:				
Revenue	$ 39,749	$ 29,951	$ 77,062	$ 59,921
Cost of revenue	14,896	12,239	28,930	24,482
Gross profit	24,853	17,712	48,132	35,439
Operating expenses				
Marketing and sales	5,550	4,557	10,813	8,998
Research and development	2,751	2,401	5,379	4,061
General and administrative	3,923	3,288	7,917	7,276
Total operating expenses	12,224	10,246	24,109	20,335
Income from operations	12,629	7,466	24,023	15,104
Other income (expense), net	116	173	119	(404)
Income before income taxes	12,745	7,639	24,142	14,700
Provision for income taxes	4,134	2,493	7,244	4,772
Net income	$ 8,611	$ 5,146	$ 16,898	$ 9,928
Net income per share:				
Basic	$ 0.34	$ 0.22	$ 0.68	$ 0.44
Diluted	$ 0.33	$ 0.20	$ 0.66	$ 0.42
Shares used to compute net income per share:				
Basic	25,258,932	23,929,886	25,030,283	22,432,415
Diluted	25,850,247	25,280,835	25,627,382	23,743,122
Comprehensive income	$ 8,413	$ 4,831	$ 15,793	$ 10,071

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

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

	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Operating activities		
Net income	$ 16,898	$ 9,928
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	3,582	2,768
Stock-based compensation expense	1,736	1,620
Deferred taxes	307	—
Excess tax benefit from stock-based compensation	(5,929)	—
Loss on disposal of property and equipment	59	—
Amortization of held-to-maturity securities	633	24
Changes in operating assets and liabilities:		
Accounts receivable	(2,032)	(2,268)
Inventories	(360)	(189)
Prepaid expenses and other	1,715	27
Income taxes	3,066	660
Accounts payable	1,083	(363)
Accrued liabilities and other	(1,310)	(705)
Net cash provided by operating activities	19,448	11,502
Investing activities		
Purchases of property and equipment	(6,069)	(12,664)
Purchases of marketable securities	(57,310)	(34,366)
Proceeds from maturities of marketable securities	34,280	250
Net cash used in investing activities	(29,099)	(46,780)
Financing activities		
Proceeds from initial public offering, net of offering costs	—	71,530
Payments on debt	(166)	(191)
Proceeds from exercises of warrants and stock options	2,870	37
Excess tax benefit from stock-based compensation	5,929	—
Net cash provided by financing activities	8,633	71,376
Effect of exchange rate changes on cash and cash equivalents	(295)	153
Net increase (decrease) in cash and cash equivalents	(1,313)	36,251
Cash and cash equivalents, beginning of period	36,759	8,135
Cash and cash equivalents, end of period	$ 35,446	$ 44,386

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

Proto Labs, Inc.
Notes to Consolidated Financial Statements
(Unaudited)

Note 1 — Basis of Presentation

The unaudited interim Consolidated Financial Statements of Proto Labs, Inc. (Proto Labs, 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. These statements are unaudited but, in the opinion of management, reflect all adjustments necessary for a fair presentation of the Company's statement 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, 2012 as filed with the Securities and Exchange Commission (SEC) on March 22, 2013.

The accompanying Consolidated Balance Sheet as of December 31, 2012 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 March 22, 2013 as referenced above.

Certain reclassifications have been made to the Consolidated Statement of Cash Flows for the six month period ending June 30, 2012 to conform to the presentation used in the June 30, 2013 Consolidated Statement of Cash Flows. The reclassifications had no effect on the increase in cash and cash equivalents as previously reported.

Note 2 — Recent Accounting Pronouncements

In February 2013, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2013-02, *Reporting of Amounts Reclassified Out of Accumulated Other Comprehensive Income* (ASU 2013-02). This accounting update generally requires entities to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, the accounting update requires entities to present, either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under U.S. GAAP to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures required under U.S. GAAP that provide additional detail about those amounts. The amendment applies to public and nonpublic companies and is to be applied prospectively. For public entities, the amendment is effective for fiscal years, and interim periods within those years, beginning after December 15, 2012. The Company adopted this accounting guidance effective January 1, 2013. The adoption of ASU 2013-02 did not have a material impact on the Company's 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 the 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 granted under stock-based compensation plans and shares committed to be purchased under the employee stock purchase plan.

Proto Labs, Inc.
Notes to Consolidated Financial Statements
(Unaudited)

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, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Net income	$ 8,611	$ 5,146	$ 16,898	$ 9,928
Basic—weighted-average shares outstanding:	25,258,932	23,929,886	25,030,283	22,432,415
Effect of dilutive securities:				
Employee stock options, warrants and other	591,315	1,350,949	597,099	1,310,707
Diluted—weighted-average shares outstanding:	25,850,247	25,280,835	25,627,382	23,743,122
Net income per share:				
Basic	$ 0.34	$ 0.22	$ 0.68	$ 0.44
Diluted	$ 0.33	$ 0.20	$ 0.66	$ 0.42

Note 4 – 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 which 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.

A summary of financial assets as of June 30, 2013 and December 31, 2012 measured at fair value on a recurring basis follows:

	June 30, 2013			December 31, 2012		
(in thousands)	Level 1	Level 2	Level 3	Level 1	Level 2	Level 3
Financial Assets:						
Cash and cash equivalents						
Money market mutual fund	$14,636	$ —	$ —	$16,164	$ —	$ —
Total	$14,636	$ —	$ —	$16,164	$ —	$ —

Proto Labs, Inc.
Notes to Consolidated Financial Statements
(Unaudited)

Note 5 – Marketable Securities

The Company invests in short-term and long-term agency, municipal, corporate, commercial paper and other debt securities. The securities are categorized as held-to-maturity and are recorded at amortized cost. Categorization as held-to-maturity is based on the Company's ability and intent to hold these securities to maturity. Information regarding the Company's short-term and long-term marketable securities as of June 30, 2013 and December 31, 2012 is as follows:

	June 30, 2013			
(in thousands)	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. government agency securities	$ 26,589	$ 4	$ (44)	$ 26,549
Corporate debt securities	23,631	12	(84)	23,559
Commercial paper	5,497	—	(5)	5,492
U.S. municipal securities	25,821	5	(64)	25,762
Certificates of deposit/time deposits	2,961	6	(6)	2,961
Total marketable securities	$ 84,499	$ 27	$ (203)	$ 84,323

	December 31, 2012			
(in thousands)	Amortized Cost	Unrealized Gains	Unrealized Losses	Fair Value
U.S. government agency securities	$ 23,011	$ 2	$ (4)	$ 23,009
Corporate debt securities	14,675	18	(14)	14,679
Commercial paper	1,500	—	—	1,500
U.S. municipal securities	17,971	3	(12)	17,962
Certificates of deposit/time deposits	4,945	3	(1)	4,947
Total marketable securities	$ 62,102	$ 26	$ (31)	$ 62,097

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

The Company tests for other than temporary losses on a quarterly basis and has considered the unrealized losses indicated above to be temporary in nature. The Company intends to hold the investments to maturity and recover the full principal.

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, 2013 balance of held-to-maturity debt securities by contractual maturity is shown in the following table at amortized cost. Actual maturities may differ from contractual maturities because the issuers of the securities may have the right to prepay obligations without prepayment penalties.

Proto Labs, Inc.
Notes to Consolidated Financial Statements
(Unaudited)

(in thousands)	June 30, 2013
Due in one year or less	$30,330
Due after one year through five years	54,169
Total marketable securities	$84,499

Note 6—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 consists of the following:

(in thousands)	June 30, 2013	December 31, 2012
Raw materials	$4,502	$ 4,174
Work in process	489	530
Total inventory	4,991	4,704
Allowance for obsolescence	(116)	(85)
Inventory, net of allowance	$4,875	$ 4,619

Note 7 – Stock-Based Compensation

Under the 2012 Long-Term Incentive Plan (2012 Plan), as discussed in the 2012 Annual Report on Form 10-K, the Company has the ability to grant stock options, stock appreciation rights (SARs), restricted stock, stock units, other stock-based awards and cash incentive awards. Awards under the 2012 Plan will 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), as discussed in the 2012 Annual Report on Form 10-K, allows eligible employees to purchase shares of the Company's common stock 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 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.

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Proto Labs, Inc.
Notes to Consolidated Financial Statements
(Unaudited)

Stock-Based Compensation Expense

Stock-based compensation expense was $0.9 million and $0.8 million for the three months ended June 30, 2013 and 2012, and $1.7 million and $1.6 million for the six months ended June 30, 2013 and 2012, respectively.

Stock Options

A summary of stock option activity for the six months ended June 30, 2013 is as follows:

	Stock Options	Weighted-Average Exercise Price
Options outstanding at December 31, 2012	1,691,357	$ 11.11
Granted	183,615	49.07
Exercised	(466,938)	5.07
Forfeited	(854)	30.58
Options outstanding at June 30, 2013	1,407,180	$ 18.05
Exercisable at June 30, 2013	556,444	$ 11.13

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 five-year period 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, 2013 was $25.57.

The following table provides the assumptions used in the Black-Scholes pricing model valuation of options:

	Six Months Ended June 30,	
	2013	2012
Risk-free interest rate	1.03 - 1.30%	0.95 - 1.16%
Expected life (years)	5.50 - 6.50	5.50 - 6.50
Expected volatility	53.32 - 53.54%	53.00 - 53.14%
Expected dividend yield	0%	0%

As of June 30, 2013, there was $8.5 million of total unrecognized compensation expense related to unvested stock options, which is expected to be recognized over a weighted-average period of 2.9 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, 2013 and 2012, respectively:

Proto Labs, Inc.
Notes to Consolidated Financial Statements
(Unaudited)

	Six Months Ended June 30, 2013	2012
Risk-free interest rate	0.11 - 0.13%	0.16%
Expected life (months)	6.00	8.50
Expected volatility	53.14 - 53.32%	53.00%
Expected dividend yield	0%	0%

Note 8 – Accumulated Other Comprehensive Income

Other comprehensive income (loss) is comprised entirely of foreign currency translation adjustments. The following table presents the changes in accumulated other comprehensive income balances during the three and six month periods ended June 30, 2013 and 2012, respectively:

(in thousands)	Three Months Ended June 30, 2013	2012	Six Months Ended June 30, 2013	2012
Foreign currency translation adjustment, net of tax				
Balance at beginning of period	$ (1,835)	$ (280)	$ (928)	$(738)
Other comprehensive income before reclassifications	(198)	(315)	(1,105)	143
Amounts reclassified from accumulated other comprehensive income	—	—	—	—
Net current-period other comprehensive income	(198)	(315)	(1,105)	143
Balance at end of period	$ (2,033)	$ (595)	$(2,033)	$(595)

Note 9—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, 2013 and 2012 the Company recorded an income tax provision of $4.1 million and $2.5 million, respectively. For the six months ended June 30, 2013 and 2012 the Company recorded an income tax provision of $7.2 million and $4.8 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, 2013 was 32.4 percent compared with 32.6 percent in the same period of the prior year. The effective income tax rate for the six months ended June 30, 2013 was 30.0 percent compared with 32.4 percent in the same period of the prior year.

The effective income tax rate for the three months ended June 30, 2013 differs from the U.S. federal statutory rate of 35 percent primarily due to the components of income. The effective income tax rate for the six months ended June 30, 2013 differs from the U.S. federal statutory rate of 35 percent primarily due to the components of income, particularly as it relates to the federal research and development credit. On January 2, 2013, the American Taxpayer Relief Act of 2012 (the Act) was signed into law, extending the research and development credit for years 2012 and 2013. As the Act was enacted during 2013, the federal portion of the 2012 research and development credit was recognized in the first quarter of 2013. The Company recorded a tax benefit of $0.3 million for the 2012 federal research credit, which translated to an effective income tax rate reduction of 1.4 percent for the six months ended June 30, 2013.

The Company has liabilities related to unrecognized tax benefits totaling $0.4 million at June 30, 2013 and December 31, 2012. There were no material adjustments to the unrecorded tax benefits during the three or six month periods ended June 30, 2013, and the Company does not anticipate that total unrecognized tax benefits will materially change in the next twelve months. 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.

Proto Labs, Inc.
Notes to Consolidated Financial Statements
(Unaudited)

Note 10—Revenue and Geographic Information

The Company's revenue is derived from its Protomold injection molding and Firstcut computer numerical control (CNC) machining product lines. Total revenue by product line is as follows:

(in thousands)	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Revenue:				
Protomold	$ 27,924	$ 21,446	$ 54,804	$ 43,239
Firstcut	11,825	8,505	22,258	16,682
Total revenue	$ 39,749	$ 29,951	$ 77,062	$ 59,921

Revenue to external customers based on the billing location of the end user customer and long-lived assets by geographic region are as follows:

(in thousands)	Three Months Ended June 30, 2013	Three Months Ended June 30, 2012	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Revenue:				
United States	$ 30,106	$ 22,905	$ 58,254	$ 45,080
International	9,643	7,046	18,808	14,841
Total revenue	$ 39,749	$ 29,951	$ 77,062	$ 59,921

(in thousands)	June 30, 2013	December 31, 2012
Long-lived assets:		
United States	$39,861	$ 37,869
International	7,283	7,447
Total long-lived assets	$47,144	$ 45,316

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

The following discussion and analysis of our financial condition and results of operations 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, 2012.

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 which 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 our 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 a leading online and technology-enabled manufacturer of quick-turn CNC-machined and injection-molded custom parts for prototyping and short-run production. We provide "Real Parts, Really Fast" to product developers worldwide, who are under increasing pressure to bring their finished products to market faster than their competition. We believe low-volume manufacturing has historically been an underserved market due to the inefficiencies inherent in the quotation, equipment set-up and non-recurring engineering processes required to produce custom parts. Our proprietary technology eliminates most of the time-consuming and expensive skilled labor conventionally required to quote and manufacture parts in low volumes, and our customers conduct nearly all of their business with us over the Internet. We target our services to the millions of product developers who use three-dimensional computer-aided design (3D CAD) software to design products across a diverse range of end-markets. Our primary manufacturing services currently include Firstcut, which is our CNC machining service, and Protomold, which is our injection molding service.

Key Financial Measures and Trends

Revenue

The Company's operations are comprised of three geographic business units in the United States, Europe and Japan. Revenue within each of our business units is derived from our Firstcut and Protomold services. Firstcut revenue consists of sales of CNC-machined custom parts. Protomold revenue consists of sales of custom injection molds and injection-molded parts. Our historical and current efforts to increase revenue have been directed at gaining new customers and selling to our existing customer base by increasing marketing and selling activities, offering additional services such as the introduction of our Firstcut service in 2007, expanding internationally such as the opening of our Japanese plant in 2009, improving the usability of our services such as our web-centric applications, and expanding the breadth and scope of our products such as by adding more sizes and materials to our offerings. During the three months ended June 30, 2013, we served approximately 6,900 unique product developers, an increase of 22% over the same period in 2012. During the six months ended June 30, 2013, we served approximately 10,200 unique product developers, an increase of 21% over the same period in 2012.

Cost of Revenue, Gross Profit and Gross Margin

Cost of revenue consists primarily of raw materials, equipment depreciation, employee salaries, benefits, stock-based compensation, bonuses and overhead allocations associated with the manufacturing process for molds and custom parts. 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 pricing, sales volume and manufacturing costs, the costs associated with increasing production capacity, the mix between domestic and foreign revenue sources and foreign exchange rates.

Our gross margins vary between geographic markets due primarily to the costs associated with starting new factories and our operating maturity in these markets. We believe that over time and with growth and maturity of our international business, gross margins will be generally consistent through all our markets.

Operating Expenses

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

Our recent growth in operating expenses is mainly due to higher headcounts to support our growth and expansion, and we expect that trend to continue. Our business strategy is to continue to be a leading online and technology-enabled manufacturer of quick-turn CNC machined and injection-molded custom parts for prototyping and short-run production. For us to achieve our goals, 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 salaries, benefits, commissions, stock-based compensation, bonuses, marketing programs such as print and pay-per-click advertising, trade shows, direct mail 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.

Research and development. Research and development expense consists primarily of employee salaries, benefits, stock-based compensation, bonuses, depreciation on equipment, outside services and other related overhead. All of our research and development costs have been expensed as incurred. We expect research and development expense to increase in the future as we seek to enhance and expand our service offerings.

General and administrative. General and administrative expense consists primarily of employee salaries, benefits, stock-based compensation, bonuses, professional service fees related to accounting, tax and legal, and other related overhead. We expect general and administrative expense to increase on an absolute basis and as a percentage of revenue as we continue to grow and expand our operations and develop the infrastructure necessary to operate as a public company. These expenses will include increased audit and legal fees, costs of compliance with securities and other regulations, implementation costs for compliance with the provisions of the Sarbanes-Oxley Act, investor relations expense and higher insurance premiums.

Other Income (Expense), net

Other income (expense), net primarily consists of foreign currency-related gains and losses, interest income on cash balances and investments, and interest expense on borrowings. 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. Our interest expense will vary based on borrowings and interest rates.

Provision for Income Taxes

Provision for income taxes is comprised of federal, state, local and foreign taxes based on pre-tax income. We expect income taxes to increase as our taxable income increases and our effective tax rate to remain relatively constant.

Results of Operations

The following table sets forth a summary of 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.

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(dollars in thousands)	Three Months Ended June 30, 2013		2012		Change $	%	Six Months Ended June 30, 2013		2012		Change $	%
Revenue	$39,749	100.0%	$29,951	100.0%	$9,798	32.7%	$77,062	100.0%	$59,921	100.0%	$17,141	28.6%
Cost of revenue	14,896	37.5	12,239	40.9	2,657	21.7	28,930	37.5	24,482	40.9	4,448	18.2
Gross profit	24,853	62.5	17,712	59.1	7,141	40.3	48,132	62.5	35,439	59.1	12,693	35.8
Operating expenses:												
Marketing and sales	5,550	13.9	4,557	15.2	993	21.8	10,813	14.0	8,998	15.0	1,815	20.2
Research and development	2,751	6.9	2,401	8.0	350	14.6	5,379	7.0	4,061	6.8	1,318	32.5
General and administrative	3,923	9.9	3,288	11.0	635	19.3	7,917	10.3	7,276	12.1	641	8.8
Total operating expenses	12,224	30.7	10,246	34.2	1,978	19.3	24,109	31.3	20,335	33.9	3,774	18.6
Income from operations	12,629	31.8	7,466	24.9	5,163	69.2	24,023	31.2	15,104	25.2	8,919	59.1
Other income (expense), net	116	0.3	173	0.6	(57)	(32.9)	119	0.1	(404)	(0.7)	523	129.5
Income before income taxes	12,745	32.1	7,639	25.5	5,106	66.8	24,142	31.3	14,700	24.5	9,442	64.2
Provision for income taxes	4,134	10.4	2,493	8.3	1,641	65.8	7,244	9.4	4,772	7.9	2,472	51.8
Net income	$ 8,611	21.7%	$ 5,146	17.2%	$3,465	67.3%	$16,898	21.9%	$ 9,928	16.6%	$ 6,970	70.2%

Stock-based compensation expense included in the statements of operations data above is as follows:

(dollars in thousands)	Three Months Ended June 30, 2013	2012	Six Months Ended June 30, 2013	2012
Stock options and grants	$ 778	$ 612	$ 1,554	$ 1,409
Employee stock purchase plan	93	158	182	211
Total stock-based compensation expense	$ 871	$ 770	$ 1,736	$ 1,620
Cost of revenue	$ 73	$ 100	$ 144	$ 145
Operating expenses:				
Marketing and sales	151	110	301	183
Research and development	181	126	354	204
General and administrative	466	434	937	1,088
Total stock-based compensation expense	$ 871	$ 770	$ 1,736	$ 1,620

Comparison of Three Months Ended June 30, 2013 and 2012

Revenue

Revenue by product line and the related changes for the three months ended June 30, 2013 and 2012 were as follows:

(dollars in thousands)	Three Months Ended June 30, 2013 $	% of Total Revenue	2012 $	% of Total Revenue	Change $	%
Revenue						
Protomold	$27,924	70.3%	$21,446	71.6%	$6,478	30.2%
Firstcut	11,825	29.7	8,505	28.4	3,320	39.0
Total revenue	$39,749	100.0%	$29,951	100.0%	$9,798	32.7%

Revenue by geographic region, based on the billing location of the end customer, is summarized as follows:

	Three Months Ended June 30,					
	2013		2012		Change	
(dollars in thousands)	$	% of Total Revenue	$	% of Total Revenue	$	%
Revenue						
United States	$30,106	75.7%	$22,905	76.5%	$7,201	31.4%
International	9,643	24.3	7,046	23.5	2,597	36.9
Total revenue	$39,749	100.0%	$29,951	100.0%	$9,798	32.7%

Our revenue increased $9.8 million, or 32.7%, for the three months ended June 30, 2013 compared with the same period in 2012. This revenue growth was driven by a 31.4% increase in United States revenue, 36.9% increase in international revenue, 30.2% increase in Protomold revenue and 39.0% increase in Firstcut revenue, in each case for the three months ended June 30, 2013 compared with the same period in 2012.

Our revenue growth in the three months ended June 30, 2013 was the result of increased volume and spending of the product developers we served. During the three months ended June 30, 2013, we served approximately 6,900 unique product developers, an increase of 22% over the same period in 2012. Average revenue per product developer also increased 8% during the three months ended June 30, 2013 compared to the same period in 2012.

Our revenue increases were primarily driven by increases in sales personnel and marketing activities. Our sales personnel focus on gaining new customer accounts and expanding the depth and breadth into existing customer accounts. Our marketing personnel focus on trade show and marketing activities that have proven to result in the greatest number of customer leads to support sales activity. International revenue was negatively impacted by $0.5 million in the three months ended June 30, 2013 compared to the same period in 2012 due to strengthening of the United States dollar relative to certain foreign currencies. The effect of pricing changes on revenue was immaterial for the three months ended June 30, 2013 compared to the same period in 2012.

Cost of Revenue, Gross Profit and Gross Margin

Cost of Revenue. Cost of revenue increased $2.7 million, or 21.7%, for the three months ended June 30, 2013 compared to the same period in 2012, which was slower than the rate of revenue increase of 32.7% for the three months ended June 30, 2013 compared to the same period in 2012. The increase in cost of revenue was due to raw material and production cost increases of $1.1 million to support increased sales volumes, equipment and facility-related cost increases of $0.5 million and an increase in direct labor headcount resulting in personnel and related cost increases of $1.1 million.

Gross Profit and Gross Margin. Gross profit increased to $24.9 million, or 62.5% of revenues, for the three months ended June 30, 2013 from $17.7 million, or 59.1% of revenues, for the three months ended June 30, 2012 due to increases in revenue offset by the cost of revenue as discussed above. Gross margin increased primarily as a result of efficiencies gained through higher equipment utilization and continually refined manufacturing processes as well as a growth rate in order volume that exceeded capacity expansion through capital equipment acquisition.

Operating Expenses, Other Income (Expense), net and Provision for Income Taxes

Marketing and Sales. Marketing and sales expense increased $1.0 million, or 21.8%, for the three months ended June 30, 2013 compared to the same period in 2012 due primarily to an increase in headcount resulting in personnel and related cost increases of $0.9 million and marketing program cost increases of $0.1 million. The increase in marketing program costs is the result of our focus and concentration on funding those programs which have proven to be the most effective in growing our business. Marketing and sales expense as a percentage of revenue decreased to 13.9% for the three months ended June 30, 2013 from 15.2% during the same period in 2012, primarily due to the fixed nature of certain marketing and sales costs as well as focus on effective marketing spending as previously discussed.

Research and Development. Our research and development expense increased $0.3 million, or 14.6%, for the three months ended June 30, 2013 compared to the same period in 2012 due to an increase in headcount resulting in personnel and related cost increases of $0.4 million and operating cost increases of $0.1 million, which were partially offset by a decrease in professional services of $0.2 million for outside development services.

General and Administrative. Our general and administrative expense increased $0.6 million, or 19.3%, for the three months ended June 30, 2013 compared to the same period in 2012 due to an increase in headcount resulting in personnel and related cost increases of $0.2 million, administrative cost increases of $0.3 million and professional service cost increases of $0.1 million. The increase in professional service costs is attributable to our becoming a public company during the first quarter of 2012.

Other Income (Expense), net. Other income, net decreased $0.1 million for the three months ended June 30, 2013 compared to the same period in 2012 due to changes in foreign currency rates.

Provision for Income Taxes. Our effective tax rate of 32.4% for the three months ended June 30, 2013 remained relatively consistent with our effective tax rate of 32.6% for the same period in 2012. As a result of increased income attributable to the fluctuations described above, our income tax provision increased by $1.6 million to $4.1 million for the three months ended June 30, 2013 compared to our income tax provision of $2.5 million for the three months ended June 30, 2012.

Comparison of Six Months Ended June 30, 2013 and 2012

Revenue

Revenue by product line and the related changes for the six months ended June 30, 2013 and 2012 were as follows:

	Six Months Ended June 30,					
	2013		2012		Change	
(dollars in thousands)	$	% of Total Revenue	$	% of Total Revenue	$	%
Revenue						
Protomold	$54,804	71.1%	$43,239	72.2%	$11,565	26.7%
Firstcut	22,258	28.9	16,682	27.8	5,576	33.4
Total revenue	$77,062	100.0%	$59,921	100.0%	$17,141	28.6%

Revenue by geographic region, based on the billing location of the end customer, is summarized as follows:

	Six Months Ended June 30,					
	2013		2012		Change	
(dollars in thousands)	$	% of Total Revenue	$	% of Total Revenue	$	%
Revenue						
United States	$58,254	75.6%	$45,080	75.2%	$13,174	29.2%
International	18,808	24.4	14,841	24.8	3,967	26.7
Total revenue	$77,062	100.0%	$59,921	100.0%	$17,141	28.6%

Our revenue increased $17.1 million, or 28.6%, for the six months ended June 30, 2013 compared with the same period in 2012. This revenue growth was driven by a 29.2% increase in United States revenue, 26.7% increase in international revenue, 26.7% increase in Protomold revenue and 33.4% increase in Firstcut revenue, in each case for the six months ended June 30, 2013 compared with the same period in 2012.

Our revenue growth in the six months ended June 30, 2013 was the result of increased volume and spending of the product developers we served. During the six months ended June 30, 2013, we served approximately 10,200 unique product developers, an increase of 21% over the same period in 2012. Average revenue per product developer also increased 6% during the six months ended June 30, 2013 compared to the same period in 2012.

Our revenue increases were primarily driven by increases in sales personnel and marketing activities. Our sales personnel focus on gaining new customer accounts and expanding the depth and breadth into existing customer accounts. Our marketing personnel focus on trade show and marketing activities that have proven to result in the greatest number of customer leads to support sales activity. International revenue was negatively impacted by $0.8 million in the six months ended June 30, 2013 compared to the same period in 2012 due to strengthening of the United States dollar relative to certain foreign currencies. The effect of pricing changes on revenue was immaterial for the six months ended June 30, 2013 compared to the same period in 2012.

Cost of Revenue, Gross Profit and Gross Margin

Cost of Revenue. Cost of revenue increased $4.4 million, or 18.2%, for the six months ended June 30, 2013 compared to the same period in 2012, which was slower than the rate of revenue increase of 28.6% for the six months ended June 30, 2013 compared to the same period in 2012. The increase in cost of revenue was due to raw material and production cost increases of $1.7 million to support increased sales volumes, equipment and facility-related cost increases of $0.9 million and an increase in direct labor headcount resulting in personnel and related cost increases of $1.8 million.

Gross Profit and Gross Margin. Gross profit increased to $48.1 million, or 62.5% of revenues, for the six months ended June 30, 2013 from $35.4 million, or 59.1% of revenues, for the six months ended June 30, 2012 due to increases in revenue offset by the cost of revenue as discussed above. Gross margin increased primarily as a result of efficiencies gained through higher equipment utilization and continually refined manufacturing processes as well as a growth rate in order volume that exceeded capacity expansion through capital equipment acquisition.

Operating Expenses, Other Income (Expense), net and Provision for Income Taxes

Marketing and Sales. Marketing and sales expense increased $1.8 million, or 20.2%, for the six months ended June 30, 2013 compared to the same period in 2012 due primarily to an increase in headcount resulting in personnel and related cost increases of $1.6 million and marketing program cost increases of $0.2 million. The increase in marketing program costs is the result of our focus and concentration on funding those programs which have proven to be the most effective in growing our business. Marketing and sales expense as a percentage of revenue decreased to 14.0% for the six months ended June 30, 2013 from 15.0% during the same period in 2012, primarily due to the fixed nature of certain marketing and sales costs as well as focus on effective marketing spending as previously discussed.

Research and Development. Our research and development expense increased $1.3 million, or 32.5%, for the six months ended June 30, 2013 compared to the same period in 2012 due to an increase in headcount resulting in personnel and related cost increases of $0.8 million, operating cost increases of $0.3 million and professional services of $0.2 million for outside development services.

General and Administrative. Our general and administrative expense increased $0.6 million, or 8.8%, for the six months ended June 30, 2013 compared to the same period in 2012 due to an increase in headcount resulting in personnel and related cost increases of $0.2 million, professional service cost increases of $0.3 million and administrative cost increases of $0.3 million, which were partially offset by a decrease in stock-based compensation costs of $0.2 million. The increase in professional service costs is attributable to our becoming a public company during the first quarter of 2012.

Other Income (Expense), net. Other income, net increased $0.5 million for the six months ended June 30, 2013 compared to the same period in 2012 due to changes in foreign currency rates.

Provision for Income Taxes. Our income tax provision increased by $2.4 million to $7.2 million while our effective tax rate decreased by 2.4% to 30.0% for the six months ended June 30, 2013 compared to income tax provision of $4.8 million and effective tax rate of 32.4% for the six months ended June 30, 2012. On January 2, 2013, the American Taxpayer Relief Act of 2012 (the Act) was signed into law, extending the research and development credit for years 2012 and 2013. As the Act was enacted during 2013, the federal portion of the 2012 research and development credit was recognized in the first quarter of 2013. We recorded a tax benefit of $0.3 million for the 2012 federal research credit, which translated to an effective income tax rate reduction of 1.4% for the six months ended June 30, 2013. The remaining decrease in effective tax rate was the result of other individually immaterial fluctuations based on the nature of our operations and mix of revenue earned in the domestic and foreign jurisdictions in which we operate.

Liquidity and Capital Resources

Cash Flows

The following table summarizes our cash flows for the six months ended June 30, 2013 and 2012:

(dollars in thousands)	Six Months Ended June 30, 2013	Six Months Ended June 30, 2012
Net cash provided by operating activities	$ 19,448	$ 11,502
Net cash used in investing activities	(29,099)	(46,780)
Net cash provided by financing activities	8,633	71,376
Effect of exchange rates on cash and cash equivalents	(295)	153
Net increase (decrease) in cash and cash equivalents	$ (1,313)	$ 36,251

Sources of Liquidity

Historically we have financed our operations and capital expenditures through operations, lease financing and the use of bank loans. In February 2012, we completed the IPO of our common stock, which provided us with $71.5 million of cash, net of underwriting discounts and commissions and offering expenses payable by us. We had cash and cash equivalents of $35.4 million as of June 30, 2013, a decrease of $1.3 million from December 31, 2012. The decrease in our cash was primarily due to investment activity described in Note 5 to the consolidated financial statements.

Cash Flows from Operating Activities

Cash provided by operating activities was $19.4 million for the six months ended June 30, 2013. We had net income of $16.9 million, which included non-cash charges consisting of $3.6 million in depreciation, $1.7 million in stock-based compensation, $0.6 million in amortization of held-to-maturity securities and $0.3 million in deferred taxes, offset by $5.9 million of excess tax benefit on stock-based compensation. Other sources of cash in operating activities totaled $2.2 million, which included an increase in income taxes payable of $3.1 million, increase in prepaid expenses and other of $1.7 million and increase in accounts payable of $1.1 million, which were partially offset by an increase in accounts receivable of $2.0 million, increase in inventories of 0.4 million and decrease in accrued liabilities and other of $1.3 million. These operating cash increases in accounts receivable, accounts payable, inventories and other reflect increases in revenue and the growth of our business.

Cash provided by operating activities was $11.5 million for the six months ended June 30, 2012. We had net income of $9.9 million, which included non-cash charges consisting of $2.8 million in depreciation and $1.6 million in stock-based compensation. Other uses of cash in operating activities totaled $2.8 million, which included an increase in accounts receivable of $2.3 million, increase in inventory of $0.2 million, decrease in accounts payable of $0.3 million and decrease in accrued liabilities of $0.7 million, which were partially offset by an increase in income taxes payable of $0.7 million. The increase in accounts receivable reflects increases in revenue.

Cash Flows from Investing Activities

Cash used in investing activities was $29.1 million for the six months ended June 30, 2013, consisting of $6.1 million for the purchase of property and equipment and $57.3 million for the purchase of marketable securities, which were partially offset by $34.3 million in proceeds from the maturities and call redemptions of marketable securities.

Cash used in investing activities was $46.8 million for the six months ended June 30, 2012, consisting of $12.7 million for the purchase of property and equipment, $34.3 million for the purchase of marketable securities and a net reduction of short-term investments of $0.2 million.

Cash Flows from Financing Activities

Cash provided by financing activities was $8.6 million for the six months ended June 30, 2013, consisting of excess tax benefit on stock-based compensation of $5.9 million and $2.9 million in proceeds from exercises of stock options, partially offset by $0.2 million for payments of debt.

Cash generated in financing activities was $71.4 million for the six months ended June 30, 2012, consisting primarily of $71.5 million from the IPO of our common stock reduced by $0.1 million for payments of debt.

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 most significant accounting policies are discussed herein.

The preparation of the consolidated financial statements, in conformity with U.S. GAAP, requires us to make estimates and assumptions that affect the amounts reported in the consolidated financial statements and accompanying Notes. Our estimates and assumptions, including those related to revenue recognition, the allowance for doubtful accounts, inventory valuation, stock-based compensation and income taxes, are updated as appropriate, which in most cases is quarterly.

We base our estimates of the carrying value of certain assets and liabilities on historical experience and on various other assumptions that we believe to be reasonable under the circumstances. In many cases, we could reasonably have used different accounting policies and estimates. In some cases, changes in the accounting estimates are reasonably likely to occur from period to period. Management has discussed the development, selection and disclosure of these estimates with the audit committee of our board of directors. Our actual results may differ significantly from these estimates under different assumptions or conditions.

We believe the following critical accounting policies affect our more significant judgments used in the preparation of our consolidated financial statements.

Revenue Recognition

We recognize revenue in accordance with ASC 605, *Revenue Recognition* (ASC 605), which states that revenue is realized or realizable and earned when all of the following criteria are met: (1) persuasive evidence of an arrangement exists, (2) delivery has occurred or services have been rendered, (3) the price to the buyer is fixed or determinable, and (4) collectability is reasonably assured.

Revenue is generally recognized upon transfer of title and risk of loss, which for us is upon shipment of parts.

Allowance for Doubtful Accounts

We carry our accounts receivable at their invoiced amount less an allowance for doubtful accounts. On a periodic basis, we evaluate our accounts receivable and establish an allowance for doubtful accounts based on the history of write-offs and collections. A receivable is considered past due if payment has not been received within the period agreed upon in the invoice. Accounts receivable are written off after all collection efforts have been exhausted. To date, we have not incurred any write-offs of accounts receivable significantly different than the amounts reserved. We believe appropriate reserves have been established, but they may not be indicative of future write-offs. Our allowance for doubtful accounts was $0.2 million as of each of June 30, 2013 and December 31, 2012. Our allowance for doubtful accounts has decreased as a percentage of accounts receivable due to improvements in account aging driven by stronger credit policies.

We also record a provision for estimated product returns and allowances in the period in which the related revenue is recorded. This provision against current gross revenue is based principally on historical rates of sales returns.

Inventory Valuation and Inventory Reserves

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, or FIFO, cost. We periodically review our inventory for slow-moving, damaged and discontinued items and provide reserves to reduce such items identified to their recoverable amounts. Our inventory allowance for obsolescence was $0.1 million as of each of June 30, 2013 and December 31, 2012.

Stock-Based Compensation

We determine our stock-based compensation in accordance with ASC 718, *Compensation—Stock Compensation* (ASC 718), which requires the measurement and recognition of compensation expense for all share-based payment awards made to employees and non-employee directors based on the grant date fair value of the award.

Determining the appropriate fair value model and calculating the fair value of stock option grants requires the input of highly subjective assumptions. We use the Black-Scholes option pricing model to value our stock option awards. Stock-based compensation expense is significant to our consolidated financial statements and is calculated using our best estimates, which involve inherent uncertainties and the application of management's judgment. Significant estimates include our expected term, stock price volatility and forfeiture rates. If different estimates and assumptions had been used, our common stock valuations could be significantly different and related stock-based compensation expense may be materially impacted.

The Black-Scholes option pricing model requires inputs such as the risk-free interest rate, expected term, expected volatility and expected dividend yield. We base the risk-free interest rate that we use in the Black-Scholes option pricing model on zero coupon U.S. Treasury instruments with maturities similar to the expected term of the award being valued. The expected term represents the weighted-average period that our stock options are expected to be outstanding. The expected term is based on the observed and expected time to post-vesting exercise of options by employees and non-employee directors and considers the impact of post-vesting award forfeitures. Because we operated as a private company with a limited market for our stock from inception to the completion of our IPO in February 2012, we estimate the volatility of our common stock based on volatility of a peer group of comparable publicly traded companies for which historical information is available. We have never paid and do not anticipate paying any cash dividends in the foreseeable future and, therefore, we use an expected dividend yield of zero in the option pricing model. In order to properly attribute compensation expense, we are required to estimate pre-vesting forfeitures at the time of grant and revise those estimates in subsequent periods if actual forfeitures differ from those estimates. We use historical data to estimate pre-vesting forfeitures and record stock-based compensation expense only for those awards that are expected to vest. If our actual forfeiture rate is materially different from our estimate, stock-based compensation expense could be significantly different from what has been recorded.

We allocate stock-based compensation expense on a straight-line basis over the requisite service period.

Income Taxes

We account for income taxes in accordance with ASC 740, *Income Taxes* (ASC 740). Under this method, the Company determines tax assets and liabilities based upon the differences between the financial statement carrying amounts and the tax basis of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to affect taxable income. The tax consequences of most events recognized in the current year's financial statements are included in determining income taxes currently payable. However, because tax laws and financial accounting standards differ in their recognition and measurement of assets, liabilities and equity, revenues, expenses, gains and losses, differences arise between the amount of taxable income and pretax financial income for a year and between the tax basis of assets or liabilities and their reported amounts in the financial statements. Because we assume that the reported amounts of assets and liabilities will be recovered and settled, respectively, a difference between the tax basis of an asset or liability and its reported amount in the balance sheet will result in a taxable or a deductible amount in some future years when the related liabilities are settled or the reported amounts of the assets are recovered, giving rise to a deferred tax asset or liability.

ASC 740 also clarifies the accounting for uncertainty in income taxes recognized in an enterprise's financial statements by defining a criterion that an individual tax position must meet for any part of the benefit of that position to be recognized in an enterprise's financial statements. Additionally, ASC 740 provides guidance on measurement, de-recognition, classification, interest and penalties, accounting in interim periods, disclosure and transition.

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.

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Foreign Currency Risk

As a result of our foreign operations, we have revenue and expenses, assets and liabilities that are denominated in foreign currencies. A number of our employees are located in Europe and Japan. Therefore, a portion of our payrolls and operating expenses are paid and incurred in the British Pound, Euro and Yen. Our operating results and cash flows are adversely impacted when the U.S. dollar depreciates relative to other foreign currencies. We have not used any forward contracts or currency borrowings to hedge our exposure to foreign currency exchange risk. Foreign currency risk can be quantified by estimating the change in cash flows resulting from a hypothetical 10% adverse change in foreign exchange rates. We believe such a change would not have a material impact on our results of operations.

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.

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

There have been no material changes from the risk factors we previously disclosed in Part I, Item 1A. "Risk Factors" in our Annual Report on Form 10-K for the year ended December 31, 2012.

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)	Amended and Restated By-Laws of Proto Labs, Inc.
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**	XBRL Instance Document
101.SCH**	XBRL Taxonomy Extension Schema Document
101.CAL**	XBRL Taxonomy Extension Calculation Linkbase Document
101.DEF**	XBRL Taxonomy Extension Definition Linkbase Document
101.LAB**	XBRL Taxonomy Extension Label Linkbase Document
101.PRE**	XBRL Taxonomy Extension Presentation Linkbase Document

(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 3.4 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.

* The certifications furnished in Exhibit 32.1 hereto are deemed to accompany this Quarterly Report on Form 10-Q and will not be deemed "filed" for purposes of Section 18 of the Securities Exchange Act of 1934, as amended. Such certifications will not be deemed to be incorporated by reference into any filings under the Securities Act of 1933, as amended, or the Securities Exchange Act of 1934, as amended, except to the extent that the registrant specifically incorporates it by reference.

** Users of this data are advised that, pursuant to Rule 406T of Regulation S-T, these interactive data files are deemed not filed or part of a registration statement or prospectus for purposes of Sections 11 or 12 of the Securities Act of 1933 or Section 18 of the Securities Exchange Act of 1934 and otherwise are not subject to liability under these sections.

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: August 6, 2013	/s/ Bradley A. Cleveland
	Bradley A. Cleveland President and Chief Executive Officer (Principal Executive Officer)
Date: August 6, 2013	/s/ John R. Judd
	John R. Judd Chief Financial Officer (Principal Financial Officer)

Exhibit 31.1

**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, Bradley A. Cleveland, 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: August 6, 2013

By: /s/ Bradley A. Cleveland
Bradley A. Cleveland
President and Chief Executive Officer
(Principal Executive Officer)

Exhibit 31.2

**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 R. Judd, 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: August 6, 2013

By: /s/ John R. Judd
John R. Judd
Chief Financial Officer
(Principal Financial Officer)

Exhibit 32.1

**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, Bradley A. Cleveland, 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, 2013 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: August 6, 2013

By:	/s/ Bradley A. Cleveland
Name:	Bradley A. Cleveland
Title:	President and Chief Executive Officer

I, John R. Judd, 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, 2013 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: August 6, 2013

By:	/s/ John R. Judd
Name:	John R. Judd
Title:	Chief Financial Officer