

USANA HEALTH SCIENCES INC
Form 10-Q
August 10, 2011
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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 July 2, 2011

OR

- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from _____ to _____

Commission file number: 0-21116

USANA HEALTH SCIENCES, INC.

(Exact name of registrant as specified in its charter)

Utah
(State or other jurisdiction
of incorporation or organization)

87-0500306
(I.R.S. Employer
Identification No.)

3838 West Parkway Blvd., Salt Lake City, Utah 84120

(Address of principal executive offices, Zip Code)

(801) 954-7100

(Registrant's telephone number, including area code)

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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes 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

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

The number of shares outstanding of the registrant's common stock as of August 1, 2011 was 15,078,394.

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USANA HEALTH SCIENCES, INC.

FORM 10-Q

For the Quarterly Period Ended July 2, 2011

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(in thousands)

	As of January 1, 2011 (1)	As of July 2, 2011 (unaudited)
ASSETS		
Current assets		
Cash and cash equivalents	\$ 24,222	\$ 24,944
Inventories	34,078	35,381
Prepaid expenses and other current assets	20,261	16,325
Deferred income taxes	1,711	2,607
Total current assets	80,272	79,257
Property and equipment, net	57,568	60,564
Goodwill	16,930	16,930
Intangible assets, net	40,616	40,105
Other assets	8,416	9,072
	\$ 203,802	\$ 205,928
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities		
Accounts payable	\$ 6,445	\$ 8,345
Other current liabilities	51,179	46,144
Total current liabilities	57,624	54,489
Other long-term liabilities	1,012	1,020
Stockholders' equity		
Common stock, \$0.001 par value; Authorized 50,000 shares, issued and outstanding 15,985 as of January 1, 2011 and 15,173 as of July 2, 2011	16	15
Additional paid-in capital	51,222	46,878
Retained earnings	90,207	98,800
Accumulated other comprehensive income	3,721	4,726
Total stockholders' equity	145,166	150,419

\$ 203,802 \$ 205,928

(1) Derived from audited financial statements

The accompanying notes are an integral part of these statements.

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USANA HEALTH SCIENCES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EARNINGS

(in thousands, except per share data)

(unaudited)

	Quarter Ended	
	July 3, 2010	July 2, 2011
Net sales	\$ 126,011	\$ 148,925
Cost of sales	22,735	26,208
Gross profit	103,276	122,717
Operating expenses:		
Associate incentives	57,065	67,760
Selling, general and administrative	29,149	33,803
Total operating expenses	86,214	101,563
Earnings from operations	17,062	21,154
Other income (expense):		
Interest income	16	54
Interest expense	(5)	(2)
Other, net	(598)	(52)
Other expense, net	(587)	
Earnings before income taxes	16,475	21,154
Income taxes	5,705	7,298
Net earnings	\$ 10,770	\$ 13,856
Earnings per common share		
Basic	\$ 0.70	\$ 0.89
Diluted	\$ 0.69	\$ 0.88
Weighted average common shares outstanding		
Basic	15,318	15,530
Diluted	15,697	15,752

The accompanying notes are an integral part of these statements.

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USANA HEALTH SCIENCES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EARNINGS

(in thousands, except per share data)

(unaudited)

	Six Months Ended	
	July 3, 2010	July 2, 2011
Net sales	\$ 245,098	\$ 292,491
Cost of sales	45,755	51,870
Gross profit	199,343	240,621
Operating expenses:		
Associate incentives	111,183	132,567
Selling, general and administrative	56,607	69,673
Total operating expenses	167,790	202,240
Earnings from operations	31,553	38,381
Other income (expense):		
Interest income	34	104
Interest expense	(26)	(8)
Other, net	(256)	5
Other income (expense), net	(248)	101
Earnings before income taxes	31,305	38,482
Income taxes	10,894	13,276
Net earnings	\$ 20,411	\$ 25,206
Earnings per common share		
Basic	\$ 1.33	\$ 1.60
Diluted	\$ 1.31	\$ 1.58
Weighted average common shares outstanding		
Basic	15,315	15,720
Diluted	15,609	15,964

The accompanying notes are an integral part of these statements.

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USANA HEALTH SCIENCES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY AND COMPREHENSIVE INCOME

Six Months Ended July 3, 2010 and July 2, 2011

(in thousands)

(unaudited)

	Shares	Common Stock Value	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
For the Six Months Ended July 3, 2010						
Balance at January 2, 2010	15,309	\$ 15	\$ 16,425	\$ 56,410	\$ 1,523	\$ 74,373
Comprehensive income						
Net earnings				20,411		20,411
Foreign currency translation adjustment, net of tax benefit of \$317					(463)	(463)
Comprehensive income						19,948
Equity-based compensation expense			4,140			4,140
Common stock issued under equity award plans, including tax benefit of \$38	10		97			97
Balance at July 3, 2010	15,319	\$ 15	\$ 20,662	\$ 76,821	\$ 1,060	\$ 98,558
For the Six Months Ended July 2, 2011						
Balance at January 1, 2011	15,985	\$ 16	\$ 51,222	\$ 90,207	\$ 3,721	\$ 145,166
Comprehensive income						
Net earnings				25,206		25,206
Foreign currency translation adjustment, net of tax expense of \$560					1,005	1,005
Comprehensive income						26,211
Equity-based compensation expense			4,802			4,802
Common stock repurchased and retired	(827)	(1)	(8,725)	(16,613)		(25,339)
Common stock issued under equity award plans, including tax benefit of \$49	15		88			88
Tax impact of cancelled vested equity awards			(509)			(509)
Balance at July 2, 2011	15,173	\$ 15	\$ 46,878	\$ 98,800	\$ 4,726	\$ 150,419

The accompanying notes are an integral part of these statements.

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USANA HEALTH SCIENCES, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(in thousands)

(unaudited)

	Six Months Ended	
	July 3, 2010	July 2, 2011
Cash flows from operating activities		
Net earnings	\$ 20,411	\$ 25,206
Adjustments to reconcile net earnings to net cash provided by operating activities		
Depreciation and amortization	3,623	4,246
Loss on sale of property and equipment	7	9
Equity-based compensation expense	4,140	4,802
Excess tax benefits from equity-based payment arrangements	(61)	(48)
Deferred income taxes	(2,240)	(1,981)
Inventory valuation	601	575
Changes in operating assets and liabilities:		
Inventories	(5,781)	(1,136)
Prepaid expenses and other assets	996	4,109
Accounts payable	1,312	1,914
Other liabilities	2,319	(6,295)
Total adjustments	4,916	6,195
Net cash provided by operating activities	25,327	31,401
Cash flows from investing activities		
Proceeds from sale of property and equipment	4	1
Purchases of property and equipment	(3,666)	(5,794)
Net cash used in investing activities	(3,662)	(5,793)
Cash flows from financing activities		
Proceeds from equity awards exercised	59	39
Excess tax benefits from equity-based payment arrangements	61	48
Repurchase of common stock		(25,339)
Payments on line of credit	(7,000)	
Net cash used in financing activities	(6,880)	(25,252)
Effect of exchange rate changes on cash and cash equivalents	(16)	366

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Net increase in cash and cash equivalents	14,769	722
Cash and cash equivalents, beginning of period	13,658	24,222
Cash and cash equivalents, end of period	\$ 28,427	\$ 24,944
<u>Supplemental disclosures of cash flow information</u>		
Cash paid during the period for:		
Interest	\$ 32	\$ 9
Income taxes	12,513	13,483

The accompanying notes are an integral part of these statements.

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USANA HEALTH SCIENCES, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(in thousands, except per share data)

(unaudited)

Organization, Consolidation, and Basis of Presentation

USANA Health Sciences, Inc. develops and manufactures high-quality nutritional and personal care products that are sold internationally through a network marketing system, which is a form of direct selling. The Consolidated Financial Statements include the accounts and operations of USANA Health Sciences, Inc. and its wholly-owned subsidiaries (collectively, the Company or USANA) in two geographic regions: North America and Asia Pacific, which is further divided into three sub-regions; Southeast Asia/Pacific, Greater China, and North Asia. North America includes the United States, Canada, Mexico, and direct sales from the United States to the United Kingdom and the Netherlands. Southeast Asia/Pacific includes Australia, New Zealand, Singapore, Malaysia, and the Philippines; Greater China includes Hong Kong, Taiwan and China; and North Asia includes Japan and South Korea. All significant inter-company accounts and transactions have been eliminated in this consolidation.

The condensed balance sheet as of January 1, 2011, derived from audited financial statements, and the unaudited interim consolidated financial information of the Company have been prepared in accordance with Article 10 of Regulation S-X promulgated by the Securities and Exchange Commission. Certain information and footnote disclosures that are normally included in financial statements that have been prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted pursuant to such rules and regulations. In the opinion of management, the accompanying interim consolidated financial information contains all adjustments, consisting of normal recurring adjustments that are necessary to present fairly the Company's financial position as of July 2, 2011 and results of operations for the quarters and six months ended July 3, 2010 and July 2, 2011. These financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto that are included in the Company's Annual Report on Form 10-K for the year ended January 1, 2011. The results of operations for the quarter and six months ended July 2, 2011, may not be indicative of the results that may be expected for the fiscal year 2011 ending December 31, 2011.

Recent Accounting Pronouncements

In May 2011, the FASB issued Accounting Standards Update No. 2011-04, Fair Value Measurement (Topic 820): Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and IFRSs (ASU 2011-04). ASU 2011-04 updates existing guidance in Topic 820 to establish common requirements for measuring fair value and for disclosing information about fair value measurements in accordance with U.S. Generally Accepted Accounting Principles (U.S. GAAP) and International Financial Reporting Standards (IFRS). ASU 2011-04 is effective prospectively for fiscal years, and interim periods, beginning after December 15, 2011. Early adoption is not permitted. The Company does not expect adoption of this standard to have a material impact on its consolidated financial statements.

In June 2011, the FASB issued Accounting Standards Update No. 2011-05, Comprehensive Income (Topic 220): Presentation of Comprehensive Income (ASU 2011-05). The objective of ASU 2011-05 is to improve the comparability, consistency, and transparency of financial reporting

and to increase the prominence of items reported in other comprehensive income. To increase the prominence of items reported in other comprehensive income and to facilitate the convergence of U.S. GAAP and IFRS, ASU 2011-05 eliminates the option to present components of other comprehensive income as part of the statement of changes in stockholders' equity. Under the amendments in this update, an entity has the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. Regardless of which option is chosen, items that are reclassified from other comprehensive income to net income must be presented on the face of the financial statements. These amendments do not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. Also, the amendments do not change the option for an entity to present components of other comprehensive income either net of related tax effects or before related tax effects, with one amount shown for the aggregate income tax expense or benefit related to the total of other comprehensive income items. ASU 2011-05 is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011. Early adoption is permitted. The Company does not expect adoption of this standard to have a material impact on its consolidated financial statements.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(in thousands, except per share data)

(unaudited)

NOTE A FAIR VALUE OF FINANCIAL INSTRUMENTS

The Company reports term deposits in accordance with established authoritative guidance, which requires a three-level valuation hierarchy for disclosure of fair value measurements. The valuation hierarchy is based upon the transparency of inputs to the valuation of an asset or liability as of the measurement date.

The three levels are defined as follows:

- Level 1 inputs are quoted market prices in active markets for identical assets or liabilities that are accessible at the measurement date.
- Level 2 inputs are from other than quoted market prices included in Level 1 that are observable for the asset or liability, either directly or indirectly.
- Level 3 inputs are unobservable and are used to measure fair value in situations where there is little, if any, market activity for the asset or liability at the measurement date.

The fair values of term deposits placed with banks are determined based on the pervasive interest rates in the market, which are also the interest rates as stated in the contracts with the banks. The Company classifies the valuation techniques that use the pervasive interest rates input as Level 2. The carrying values of these term deposits approximate their fair values due to their short-term maturities. As of July 2, 2011, the fair value of term deposits in the consolidated balance sheet totaled \$1,856, consisting of \$309, classified in cash and cash equivalents, and \$1,547 in prepaid expenses and other current assets.

NOTE B INVENTORIES

Inventories consist of the following:

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	January 1, 2011		July 2, 2011
Raw materials	\$ 9,372	\$	9,931
Work in progress	5,791		5,821
Finished goods	18,915		19,629
	\$ 34,078	\$	35,381

NOTE C PREPAID EXPENSES AND OTHER CURRENT ASSETS

Prepaid expenses and other current assets consist of the following:

	January 1, 2011		July 2, 2011
Prepaid insurance	\$ 1,175	\$	660
Other prepaid expenses	2,583		3,501
Federal income taxes receivable	3,108		1,741
Miscellaneous receivables, net	3,735		3,067
Deferred commissions	4,867		3,535
Term deposits	3,034		1,547
Other current assets	1,759		2,274
	\$ 20,261	\$	16,325

Table of Contents**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS** (continued)

(in thousands, except per share data)

(unaudited)

NOTE D PROPERTY AND EQUIPMENT

Cost of property and equipment and their estimated useful lives is as follows:

	Years	January 1, 2011	July 2, 2011
Buildings	40	\$ 38,732	\$ 39,466
Laboratory and production equipment	5-7	17,723	18,517
Sound and video library	5	600	600
Computer equipment and software	3-5	27,788	29,780
Furniture and fixtures	3-5	4,953	4,904
Automobiles	3-5	290	292
Leasehold improvements	3-5	5,404	5,533
Land improvements	15	2,051	2,063
		97,541	101,155
Less accumulated depreciation and amortization		48,298	51,898
		49,243	49,257
Land		8,107	8,443
Deposits and projects in process		218	2,864
		\$ 57,568	\$ 60,564

NOTE E OTHER CURRENT LIABILITIES

Other current liabilities consist of the following:

	January 1, 2011	July 2, 2011
Associate incentives	\$ 11,379	\$ 12,453

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Accrued employee compensation	14,395	8,645
Income Taxes	1,571	1,731
Sales taxes	4,671	4,302
Associate promotions	1,491	1,417
Deferred revenue	11,772	9,422
Provision for returns and allowances	929	898
All other	4,971	7,276
	\$ 51,179	\$ 46,144

Table of Contents**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS** (continued)

(in thousands, except per share data)

(unaudited)

NOTE F EQUITY BASED COMPENSATION

Equity-based compensation expense for the quarters ended July 3, 2010, and July 2, 2011, was \$2,184 and \$1,567, respectively. The related tax benefit for these periods was \$787 and \$568, respectively. Expense for the six months ended July 3, 2010, and July 2, 2011, was \$4,140 and \$4,802, respectively. The related tax benefit for these periods was \$1,514 and \$1,751, respectively.

During the quarter ended July 2, 2011, certain executives left the Company, which resulted in the cancellation of these executives' equity awards. The recapture of equity compensation expense related to the cancellation of unvested equity awards reduced equity-based compensation expense for the quarter and six months ended July 2, 2011 by \$1,230. The related tax impact for these cancellations was \$424.

The following table shows the remaining unrecognized compensation expense on a pre-tax basis for all types of equity awards that were outstanding as of July 2, 2011. This table does not include an estimate for future grants that may be issued.

Remainder of 2011	\$	5,480
2012		9,083
2013		5,457
2014		3,419
2015 and beyond		1,611
	\$	25,050

The cost above is expected to be recognized over a weighted-average period of 2.1 years.

During the quarter ended July 2, 2011, the Company's shareholders approved a 5,000 increase in the number of new shares authorized for issuance under the Company's 2006 Equity Incentive Award Plan (the "2006 Plan"). This increase brings the total shares authorized under the 2006 Plan to 10,000. The 2006 Plan is currently the only plan utilized by the Company for the issuance of equity awards. As of July 2, 2011, a total of 4,971 units had been issued under this plan, comprising 4,849 stock-settled stock appreciation rights, 114 deferred stock units, and 8 stock options. Also, as of July 2, 2011, 761 units had been cancelled and added back to the number of units available for issuance under the 2006 Plan.

Table of Contents**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS** (continued)

(in thousands, except per share data)

(unaudited)

NOTE F EQUITY BASED COMPENSATION CONTINUED

A summary of the Company's stock option and stock-settled stock appreciation right activity for the six months ended July 2, 2011 is as follows:

	Shares	Weighted- average grant price	Weighted- average remaining contractual term	Aggregate intrinsic value*
Outstanding at January 1, 2011	4,047	\$ 32.46	3.5	\$ 45,263
Granted	25	39.31		
Exercised	(57)	28.66		
Canceled or expired	(558)	31.74		
Outstanding at July 2, 2011	3,457	\$ 32.69	3.1	\$ 13,672
Exercisable at July 2, 2011	1,209	\$ 33.37	2.7	\$ 4,385

* Aggregate intrinsic value is defined as the difference between the current market value at the reporting date (the closing price of the Company's common stock on the last trading day of the period) and the exercise price of awards that were in-the-money. The closing price of the Company's common stock at January 1, 2011 and July 2, 2011, was \$43.45 and \$33.54, respectively.

The weighted-average fair value of stock-settled stock appreciation rights that were granted during the six-month periods ended July 3, 2010, and July 2, 2011 was \$15.50 and \$17.47, respectively. The total intrinsic value of awards that were exercised during the six-month periods ended July 3, 2010, and July 2, 2011 was \$246 and \$555, respectively.

The following table includes weighted-average assumptions that the Company has used to calculate the fair value of equity awards that were granted during the periods indicated. Deferred stock units are full-value shares at the date of grant and have been excluded from the table below:

	Quarter Ended		Six Months Ended	
	July 3, 2010	July 2, 2011	July 3, 2010	July 2, 2011
Expected volatility	54.8%	*	54.9%	54.8%

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Risk-free interest rate	2.0%	*	2.0%	1.5%
Expected life	4.2 yrs.	*	4.2 yrs.	4.2 yrs.
Expected dividend yield		*		
Weighted-average grant price	\$35.47	*	\$34.46	\$39.31

* No equity awards were issued during the quarter ended July 2, 2011.

Table of Contents**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS** (continued)

(in thousands, except per share data)

(unaudited)

NOTE G COMMON STOCK AND EARNINGS PER SHARE

Basic earnings per share are based on the weighted-average number of shares outstanding for each period. Shares that have been repurchased and retired during the periods specified below have been included in the calculation of the number of weighted-average shares that are outstanding for the calculation of basic earnings per share. Diluted earnings per common share are based on shares that are outstanding (computed under basic EPS) and on potentially dilutive shares. Shares that are included in the diluted earnings per share calculations under the treasury stock method include equity awards that are in-the-money but have not yet been exercised.

	Quarters Ended	
	July 3, 2010	July 2, 2011
Net earnings available to common shareholders	\$ 10,770	\$ 13,856
<u>Basic EPS</u>		
Shares		
Common shares outstanding entire period	15,309	15,985
Weighted average common shares:		
Issued during period	9	13
Canceled during period		(468)
Weighted average common shares outstanding during period	15,318	15,530
Earnings per common share from net earnings - basic	\$ 0.70	\$ 0.89
<u>Diluted EPS</u>		
Shares		
Weighted average common shares outstanding during period - basic	15,318	15,530
Dilutive effect of in-the-money equity awards	379	222
Weighted average common shares outstanding during period - diluted	15,697	15,752
Earnings per common share from net earnings - diluted	\$ 0.69	\$ 0.88

Equity awards for 1,256 and 1,620 shares of stock were not included in the computation of diluted EPS for the quarters ended July 3, 2010, and July 2, 2011, respectively, due to the fact that their exercise prices were greater than the average market price of the shares.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (continued)

(in thousands, except per share data)

(unaudited)

NOTE G COMMON STOCK AND EARNINGS PER SHARE CONTINUED

	Six Months Ended	
	July 3, 2010	July 2, 2011
Net earnings available to common shareholders	\$ 20,411	\$ 25,206
<u>Basic EPS</u>		
Shares		
Common shares outstanding entire period	15,309	15,985
Weighted average common shares:		
Issued during period	6	8
Canceled during period		(273)
Weighted average common shares outstanding during period	15,315	15,720