Houston Wire & Cable CO
Form 10-Q
August 09, 2016

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

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

For the quarterly period ended June 30, 2016

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: 000-52046

(Exact name of registrant as specified in its charter)

Delaware	**36-4151663**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

10201 North Loop East

Houston, Texas	**77029**
(Address of principal executive offices)	(Zip Code)

(713) 609-2100

(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 x 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 x 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 definition of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act

Large Accelerated Filer ¨ Accelerated Filer x 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 x

At August 1, 2016 there were 16,470,249 outstanding shares of the registrant's common stock, $0.001 par value per share.

HOUSTON WIRE & CABLE COMPANY

Form 10-Q

For the Quarter Ended June 30, 2016

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HOUSTON WIRE & CABLE COMPANY

Consolidated Balance Sheets

(In thousands, except share data)

	June 30, 2016 (unaudited)	December 31, 2015
Assets		
Current assets:		
Accounts receivable, net	$ 41,505	$ 46,250
Inventories, net	64,580	75,777
Deferred income taxes	3,591	3,074
Income taxes	1,139	932
Prepaids	1,384	648
Total current assets	112,199	126,681
Property and equipment, net	10,814	10,899
Intangible assets, net	5,138	5,984
Goodwill	12,504	14,866
Deferred income taxes	442	264
Other assets	424	419
Total assets	$ 141,521	$ 159,113
Liabilities and stockholders' equity		
Current liabilities:		
Book overdraft	$ 491	$ 3,701
Trade accounts payable	8,352	6,380
Accrued and other current liabilities	7,800	9,568
Total current liabilities	16,643	19,649
Debt	30,092	39,188
Other long term obligations	511	275
Total liabilities	47,246	59,112
Stockholders' equity:		
Preferred stock, $0.001 par value; 5,000,000 shares authorized, none issued and outstanding	—	—
Common stock, $0.001 par value; 100,000,000 shares authorized: 20,988,952 shares issued: 16,490,559 and 16,712,626 outstanding at June 30, 2016 and December 31, 2015, respectively	21	21
Additional paid-in-capital	54,847	54,621
Retained earnings	101,308	106,048
Treasury stock	(61,901)	(60,689)
Total stockholders' equity	94,275	100,001

Total liabilities and stockholders' equity	$ 141,521	$ 159,113

The accompanying Notes are an integral part of these Consolidated Financial Statements.

HOUSTON WIRE & CABLE COMPANY

Consolidated Statements of Operations

(Unaudited)

(In thousands, except share and per share data)

	Three Months Ended June 30, 2016	2015	Six Months Ended June 30, 2016	2015
Sales	$62,454	$77,959	$127,165	$159,559
Cost of sales	50,024	61,024	101,336	124,900
Gross profit	12,430	16,935	25,829	34,659
Operating expenses:				
Salaries and commissions	6,838	7,168	13,747	14,406
Other operating expenses	5,496	6,281	11,333	12,329
Depreciation and amortization	774	726	1,466	1,438
Impairment charge	2,384	2,994	2,384	2,994
Total operating expenses	15,492	17,169	28,930	31,167
Operating income (loss)	(3,062)	(234)	(3,101)	3,492
Interest expense	149	217	324	482
Income (loss) before income taxes	(3,211)	(451)	(3,425)	3,010
Income tax expense (benefit)	(654)	168	(684)	1,443
Net income (loss)	$(2,557)	$(619)	$(2,741)	$1,567
Earnings (loss) per share:				
Basic	$(0.16)	$(0.04)	$(0.17)	$0.09
Diluted	$(0.16)	$(0.04)	$(0.17)	$0.09
Weighted average common shares outstanding:				
Basic	16,383,630	17,101,952	16,432,376	17,198,927
Diluted	16,383,630	17,101,952	16,432,376	17,251,178
Dividend declared per share	$0.06	$0.12	$0.12	$0.24

The accompanying Notes are an integral part of these Consolidated Financial Statements.

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HOUSTON WIRE & CABLE COMPANY

Consolidated Statements of Cash Flows

(Unaudited)

(In thousands)

	Six Months Ended June 30, 2016	2015
Operating activities		
Net income (loss)	$(2,741)	$1,567
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Impairment charge	2,384	2,994
Depreciation and amortization	1,466	1,438
Amortization of unearned stock compensation	422	463
Provision for inventory obsolescence	357	330
Deferred income taxes	(695)	(670)
Other non-cash items	27	83
Changes in operating assets and liabilities:		
Accounts receivable	4,738	8,564
Inventories	10,840	12,359
Book overdraft	(3,210)	(1,883)
Trade accounts payable	1,972	2,783
Accrued and other current liabilities	(1,757)	(4,009)
Income taxes	(207)	(1,069)
Other operating activities	(525)	(520)
Net cash provided by operating activities	13,071	22,430
Investing activities		
Expenditures for property and equipment	(557)	(1,545)
Net cash used in investing activities	(557)	(1,545)
Financing activities		
Borrowings on revolver	124,312	151,366
Payments on revolver	(133,408)	(164,874)
Payment of dividends	(1,990)	(4,110)
Purchase of treasury stock	(1,428)	(3,267)
Net cash used in financing activities	(12,514)	(20,885)
Net change in cash	—	—
Cash at beginning of period	—	—
Cash at end of period	$—	$—

The accompanying Notes are an integral part of these Consolidated Financial Statements.

HOUSTON WIRE & CABLE COMPANY
Notes to Consolidated Financial Statements

(Unaudited)

1. Basis of Presentation and Principles of Consolidation

Houston Wire & Cable Company (the "Company"), through its wholly owned subsidiaries, provides wire and cable, hardware and related services to the U.S. market through eighteen locations in thirteen states throughout the United States. The Company has no other business activity.

The consolidated financial statements as of June 30, 2016 and for the six months ended June 30, 2016 and 2015 have been prepared following accounting principles generally accepted in the United States ("GAAP") for interim financial information and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, considered necessary for a fair presentation of the results of these interim periods have been included. The results of operations for the interim periods are not necessarily indicative of the results that may be expected for the full year. All significant inter-company balances and transactions have been eliminated. The Company has evaluated subsequent events through the time these financial statements in this Form 10-Q were filed with the Securities and Exchange Commission (the "SEC").

The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. The most significant estimates are those relating to the inventory obsolescence reserve, the reserve for returns and allowances, vendor rebates and asset impairments. Actual results could differ materially from the estimates and assumptions used for the preparation of the financial statements.

For further information, refer to the consolidated financial statements and footnotes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2015 filed with the SEC.

Recent Accounting Pronouncements

The Financial Accounting Standards Board (the "FASB") Accounting Standards Codification ("ASC") is the sole source of authoritative GAAP other than SEC issued rules and regulations that apply only to SEC registrants. The FASB issues an Accounting Standard Update ("ASU") to communicate changes to the codification. The Company considers the applicability and impact of all ASUs. The following recently issued ASUs are relevant to the Company.

In March 2016, the FASB issued ASU No. 2016-09, “Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting.” The new guidance addresses several aspects of the accounting for share-based payment award transactions, including: (a) the recognition of the income tax effects of awards in the income statement when the awards vest, forfeit, or are settled, thus eliminating additional paid-in-capital pools, (b) classification of awards as either equity or liabilities, and (c) classification on the statement of cash flows. This update is effective for public companies for fiscal years beginning after December 15, 2016 with early adoption permitted. The Company is currently evaluating the elections the Company may make as well as the effects the adoption of this guidance may have on the Company's consolidated financial statements and determining the timing of adoption.

In February 2016, the FASB issued ASU No. 2016-02, “Leases (Topic 842).” Under the new guidance, a lessee will be required to recognize assets and liabilities for leases greater than 1 year, regardless of whether they were previously accounted for as capital or operating leases. This update is effective for public companies for fiscal years beginning after December 15, 2018 with early adoption permitted. The Company is currently evaluating the impacts of adopting as well as the timing of when it will adopt this ASU.

In November 2015, the FASB issued ASU No. 2015-17, “Income Taxes (Topic 740) — Balance Sheet Classification of Deferred Taxes.” ASU No. 2015-17 eliminates the requirement to classify deferred tax assets and liabilities as current or long-term based on how the related assets or liabilities are classified. All deferred taxes are now required to be classified as long-term including any associated valuation allowances. This guidance is effective for public companies for fiscal years beginning after December 15, 2016 with early adoption permitted on either a prospective or retrospective basis. The Company is currently evaluating the timing and method of adoption of this ASU, which impacts only the balance sheet presentation.

In July 2015, the FASB issued ASU No. 2015-11, “Simplifying the Measurement of Inventory (Topic 330),” which changes guidance for subsequent measurement of inventory within the scope of the update from the lower of cost or market to the lower of cost and net realizable value. This update is effective for annual and interim periods beginning after December 15, 2016 and early adoption is permitted. The Company does not believe there will be any material impact upon the adoption of this guidance on the Company's consolidated financial statements and is still determining the timing of adoption.

In April 2015, the FASB issued ASU No. 2015-03, "Simplifying the Presentation of Debt Issuance Costs (Subtopic 835-30)." The amendments in this ASU require debt issuance costs to be presented on the balance sheet as a direct reduction from the carrying amount of the related debt liability. However, the guidance in this ASU did not address the presentation or subsequent measurement of debt issuance costs related to line-of-credit arrangements. As a result, in August 2015 the FASB issued ASU No. 2015-15 "Interest—Imputation of Interest (Subtopic 835-30): Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Agreements," to clarify that, with respect to a line-of-credit agreement, the SEC staff would not object to an entity deferring and presenting debt issuance costs as an asset and subsequently amortizing the deferred debt issuance costs ratably over the term of the line-of-credit arrangement. The Company adopted this guidance in the first quarter and will continue to treat debt issuance costs as a deferred asset and amortize the deferred asset over the term of the credit agreement. Therefore, the adoption did not have any impact on the Company's financial position or results of operations.

In May 2014, the FASB issued ASU No. 2014-09, "Revenue from Contracts with Customers (Topic 606)," which supersedes the revenue recognition requirements in ASC Topic 605, "Revenue Recognition," and most industry-specific guidance. This ASU is based on the principle that revenue is recognized to depict the transfer of goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The ASU also requires additional disclosure about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts, including significant judgments and changes in judgments, and assets recognized from costs incurred to obtain or fulfill a contract. The amendments in the ASU must be applied using one of two retrospective methods and are effective for annual and interim periods beginning after December 15, 2017. Early adoption for annual and interim periods beginning after December 31, 2016 is permitted. The Company is still evaluating the impact of this ASU on its financial position and results of operations, timing of adoption, and which implementation method the Company will use.

2. Earnings (loss) per Share

Basic earnings (loss) per share are calculated by dividing net income (loss) by the weighted average number of common shares outstanding. Diluted earnings (loss) per share include the dilutive effects of stock options and unvested restricted stock awards and units.

The following reconciles the denominator used in the calculation of diluted earnings (loss) per share:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2016	2015	2016	2015
Denominator:				
Weighted average common shares for basic earnings (loss) per share	16,383,630	17,101,952	16,432,376	17,198,927
Effect of dilutive securities	—	—	—	52,251

Weighted average common shares for diluted earnings (loss) per share	16,383,630	17,101,952	16,432,376	17,251,178

The weighted average common shares for diluted earnings (loss) per share exclude stock options and unvested restricted stock awards and units to purchase 728,535 and 600,364 shares for the three months ended June 30, 2016 and 2015, respectively, and 697,688 and 591,436 shares for the six months ended June 30, 2016 and 2015. These securities have been excluded from the calculation, as including them would have an anti-dilutive effect on earnings (loss) per share for the respective periods.

3. Impairment of Goodwill and Intangibles

During the second quarter of 2016 and prior to the annual impairment test of goodwill in October, the Company concluded that impairment indicators existed at the Houston Wire & Cable (HWC) reporting unit, due to a decline in the overall financial performance, decrease in the market capitalization and overall market demand. The Company also concluded that there were impairment indicators for certain of the Company's tradenames related to the Southwest and Southern Wire reporting units.

The Company performed step one of the impairment test and concluded that the fair value of the HWC reporting unit was less than its carrying value. Therefore, the Company performed step two of the impairment analysis. The step one test also indicated that one of the tradenames at Southern Wire was impaired, and the Company has recorded a non-cash charge of less than $0.1 million against the tradenames during the period ended June 30, 2016.

Step two of the impairment analysis measures the impairment charge by allocating the HWC reporting unit's fair value to all of the assets and liabilities of the reporting unit in a hypothetical analysis that calculates implied fair value of goodwill in the same manner as if the reporting unit was being acquired in a business combination and recording the deferred tax impact. Any excess of the carrying value of the reporting unit's goodwill over the implied fair value of the reporting unit's goodwill is recorded as an impairment loss.

The fair value of the HWC reporting unit was estimated using a discounted cash flow model and a guideline public company method, 50% weight of each. The material assumptions used included a weighted average cost of capital of 11.0% and a long-term growth rate of 3-7% for the income approach and adjusted invested capital multiple of 0.2 times revenue and a control premium of 10.0% for the guideline public company method. The carrying value of the HWC reporting unit's goodwill was $2.4 million and its implied fair value resulting from step two of the impairment test was zero. As a result, the Company has recorded a non-cash goodwill impairment charge of $2.4 million during the period ended June 30, 2016.

The fair value for goodwill and tradenames (indefinite-lived intangible assets) were both determined using a Level 3 measurement approach. The Level 3 value of all of the Company's tradenames at June 30, 2016 was $4.5 million.

During the second quarter of 2015 and prior to the annual impairment test of goodwill in October, the Company concluded that impairment indicators existed at the Southwest Wire Rope (Southwest) reporting unit, due to a decline in the overall financial performance and overall market demand. Impairment indicators also existed for certain of the Company's tradenames related to the Southwest and Southern Wire reporting units.

After performing the necessary analysis the Company recorded, during the period ended June 30, 2015, a non-cash charge of $0.4 million against the tradenames and a non-cash goodwill impairment charge of $2.6 million.

4. Debt

On October 1, 2015, HWC Wire & Cable Company, as borrower, entered into the Fourth Amended and Restated Loan and Security Agreement (the “2015 Loan Agreement”), with Bank of America, N.A., as agent and lender, and the Company, as guarantor, executed a Third Amended and Restated Guaranty of the borrower’s obligations thereunder. The 2015 Loan Agreement provides a $100 million revolving credit facility, bears interest at the agent’s base rate, with a London Interbank Offered Rate (“LIBOR”) rate option, and expires on September 30, 2020. Under certain circumstances, the Company may request an increase in the commitment by an additional $50 million. The 2015 Loan Agreement is secured by substantially all of the property of the Company, other than real estate. Availability under the 2015 Loan Agreement is limited to a borrowing base equal to 85% of the value of eligible accounts receivable, plus the lesser of 70% of the value of eligible inventory or 90% of the net orderly liquidation value percentage of the value of eligible inventory, in each case less certain reserves.

Portions of the loan may be converted to LIBOR loans in minimum amounts of $1.0 million and integral multiples of $0.1 million. LIBOR loans bear interest at the British Bankers Association LIBOR Rate plus 100 to 150 basis points based on availability, and loans not converted to LIBOR loans bear interest at a fluctuating rate equal to the greatest of the agent’s prime rate, the federal funds rate plus 50 basis points, or 30-day LIBOR plus 150 basis points. The unused commitment fee is 25 basis points.

The 2015 Loan Agreement includes, among other things, covenants that require the Company to maintain a specified minimum fixed charge coverage ratio, unless certain availability levels exist. Additionally, the 2015 Loan Agreement allows for the unlimited payment of dividends and repurchases of stock, subject to the absence of events of default and maintenance of a fixed charge coverage ratio and minimum level of availability. The 2015 Loan Agreement contains certain provisions that may cause the debt to be classified as a current liability, in accordance with GAAP, if availability falls below certain thresholds, even though the ultimate maturity date under the loan agreement remains as September 30, 2020. At June 30, 2016, the Company was in compliance with the availability-based covenants governing its indebtedness.

The carrying amount of long term debt approximates fair value as it bears interest at variable rates. The fair value is a Level 2 measurement as defined in ASC Topic 820, “Fair Value Measurement.”

5. Stockholders’ Equity

During each of the first and second quarters of 2016, the Board of Directors approved a quarterly dividend of $0.06 per share payable to stockholders. Dividends paid were $2.0 million and $4.1 million during the six months ended June 30, 2016 and 2015, respectively.

6. Stock Based Compensation

Stock Option Awards

There were no stock option awards granted during the first six months of 2016 or 2015.

Restricted Stock Awards and Restricted Stock Units

Following the Annual Meeting of Stockholders on May 3, 2016, the Company awarded restricted stock units with a value of $50,000 to each non-employee director who was elected or re-elected, for an aggregate of 35,515 restricted stock units. Each award of restricted stock units vests at the date of the 2017 Annual Meeting of Stockholders. Each non-employee director is entitled to receive a number of shares of the Company's common stock equal to the number of vested restricted stock units, together with dividend equivalents from the date of grant, at such time as the director’s service on the board terminates for any reason.

Total stock-based compensation cost was $0.2 million for each of the three months ended June 30, 2016 and 2015 and $0.4 million and $0.5 million for the six months ended June 30, 2016 and 2015, respectively, and is included in salaries and commissions.

7. Commitments and Contingencies

As part of the acquisition of Southwest Wire Rope and Southern Wire made in 2010, the Company assumed the liability for the post-remediation monitoring of the water quality at one of the acquired facilities in Louisiana. The expected liability of $0.1 million at June 30, 2016 relates to the cost of the monitoring, which the Company estimates will be incurred over approximately the next two years, and also the cost to plug the wells. Remediation work was completed prior to the acquisition in accordance with the requirements of the Louisiana Department of Environmental Quality.

The Company has issued letters of credit totaling $2.6 million to certain vendors, of which $2.5 million will expire in October 2016.

The Company, along with many other defendants, has been named in a number of lawsuits in the state courts of Minnesota, North Dakota, and South Dakota alleging that certain wire and cable which may have contained asbestos caused injury to the plaintiffs who were exposed to this wire and cable. These lawsuits are individual personal injury suits that seek unspecified amounts of money damages as the sole remedy. It is not clear whether the alleged injuries occurred as a result of the wire and cable in question or whether the Company, in fact, distributed the wire and cable alleged to have caused any injuries. The Company maintains general liability insurance that, to date, has covered the defense of and all costs associated with these claims. In addition, the Company did not manufacture any of the wire and cable at issue, and the Company would rely on any warranties from the manufacturers of such cable if it were determined that any of the wire or cable that the Company distributed contained asbestos which caused injury to any of these plaintiffs. In connection with ALLTEL's sale of the Company in 1997, ALLTEL provided indemnities with respect to costs and damages associated with these claims that the Company believes it could enforce if its insurance coverage proves inadequate.

There are no legal proceedings pending against or involving the Company that, in management's opinion, based on the current known facts and circumstances, are expected to have a material adverse effect on the Company's consolidated financial position, cash flows, or results from operations.

8. Subsequent Events

On August 5, 2016, the Board of Directors approved a dividend on the shares of common stock of the Company in the amount of $0.03 per share, payable on August 30, 2016, to stockholders of record at the close of business on August 19, 2016.