CHEESECAKE FACTORY INC
Form 10-Q
August 05, 2010
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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 29, 2010

or

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

Commission File Number: 0-20574

THE CHEESECAKE FACTORY INCORPORATED

(Exact name of registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	**51-0340466** (I.R.S. Employer Identification No.)
26901 Malibu Hills Road **Calabasas Hills, California** (Address of principal executive offices)	**91301** (Zip Code)

(818) 871-3000

(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 o

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 o

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 x	Accelerated filer o
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes o No x

As of July 30, 2010, 59,492,511 shares of the registrant s Common Stock, \$.01 par value, were outstanding.

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THE CHEESECAKE FACTORY INCORPORATED AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

THE CHEESECAKE FACTORY INCORPORATED AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(In thousands, except share data)

	June 29, 2010 (unaudited)	December 29, 2009
ASSETS		
Current assets:		
Cash and cash equivalents	$ 86,293	$ 73,715
Accounts receivable	6,269	11,352
Income tax receivable	10,825	1,875
Other receivables	15,008	27,475
Inventories	26,788	22,202
Prepaid expenses	25,857	27,871
Deferred income taxes	7,160	7,737
Total current assets	178,200	172,227
Property and equipment, net	770,254	788,402
Other assets:		
Trademarks	4,417	4,338
Prepaid rent	52,256	54,243
Other	28,329	27,541
Total other assets	85,002	86,122
Total assets	$ 1,033,456	$ 1,046,751
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable	$ 31,650	$ 33,948
Other accrued expenses	150,147	166,513
Total current liabilities	181,797	200,461
Deferred income taxes	92,730	87,048
Deferred rent	65,570	64,209
Deemed landlord financing liability	52,639	51,802
Long-term debt	70,000	100,000
Other noncurrent liabilities	23,791	27,118
Commitments and contingencies		
Stockholders equity:		
Preferred stock, $.01 par value, 5,000,000 shares authorized; none issued	—	—
Junior participating cumulative preferred stock, $.01 par value, 150,000 shares authorized; none issued	—	—
Common stock, $.01 par value, 250,000,000 shares authorized; 84,067,900 and 83,377,092 issued at June 29, 2010 and December 29, 2009, respectively	841	834
Additional paid-in capital	404,803	386,562
Retained earnings	677,439	639,544
Accumulated other comprehensive loss	—	(4,619)
	(536,154)	(506,208)

Treasury stock, 24,257,237 and 23,100,079 shares at cost at June 29, 2010 and December 29, 2009, respectively				
Total stockholders equity		546,929		516,113
Total liabilities and stockholders equity	$	1,033,456	$	1,046,751

See the accompanying notes to the consolidated financial statements.

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THE CHEESECAKE FACTORY INCORPORATED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

(Unaudited)

	Thirteen Weeks Ended June 29, 2010	Thirteen Weeks Ended June 30, 2009	Twenty-Six Weeks Ended June 29, 2010	Twenty-Six Weeks Ended June 30, 2009
Revenues	$ 418,909	$ 407,944	$ 824,342	$ 800,738
Costs and expenses:				
Cost of sales	102,752	99,284	201,355	197,370
Labor expenses	136,038	135,143	271,207	268,383
Other operating costs and expenses	100,391	99,259	199,702	201,013
General and administrative expenses	23,766	26,075	47,190	47,485
Depreciation and amortization expenses	18,026	18,755	36,181	37,358
Preopening costs	641	469	2,735	2,189
Total costs and expenses	381,614	378,985	758,370	753,798
Income from operations	37,295	28,959	65,972	46,940
Interest expense	(10,547)	(7,459)	(13,556)	(12,489)
Interest income	17	101	168	309
Other income, net	191	630	537	455
Income before income taxes	26,956	22,231	53,121	35,215
Income tax provision	7,727	5,662	15,226	8,627
Net income	$ 19,229	$ 16,569	$ 37,895	$ 26,588
Net income per share:				
Basic	$ 0.32	$ 0.28	$ 0.64	$ 0.45
Diluted	$ 0.32	$ 0.28	$ 0.62	$ 0.44
Weighted average shares outstanding:				
Basic	59,238	59,337	59,261	59,326
Diluted	60,863	60,069	60,706	59,795

See the accompanying notes to the consolidated financial statements.

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THE CHEESECAKE FACTORY INCORPORATED AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF STOCKHOLDERS EQUITY

(In thousands)

(Unaudited)

	Shares of Common Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income/(Loss)	Treasury Stock	Total
Balance, December 29, 2009	83,377	$ 834	$ 386,562	$ 639,544	$ (4,619)	$ (506,208)	$ 516,113
Comprehensive income:							
Net income				37,895			37,895
Net unrealized loss on derivative financial instrument					41		41
Loss reclassified into income due to cancellation of derivative financial instrument					4,578		4,578
Total comprehensive income							42,514
Issuance of common stock from stock options exercised	587	6	11,581				11,587
Tax impact of stock options exercised, net of cancellations			(53)				(53)
Stock-based compensation			6,713				6,713
Issuance of restricted stock, net of forfeitures	104	1					1
Purchase of treasury stock						(29,946)	(29,946)
Balance, June 29, 2010	84,068	$ 841	$ 404,803	$ 677,439	$	$ (536,154)	$ 546,929

See the accompanying notes to the consolidated financial statements.

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THE CHEESECAKE FACTORY INCORPORATED AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Twenty-Six Weeks Ended June 29, 2010	Twenty-Six Weeks Ended June 30, 2009
Cash flows from operating activities:		
Net income	$ 37,895	$ 26,588
Adjustments to reconcile net income to cash provided by operating activities:		
Depreciation and amortization	36,181	37,358
Realized loss on derivative financial instrument	7,376	3,250
Deferred income taxes	351	(1,723)
Stock-based compensation	6,582	7,066
Tax impact of stock options exercised, net of cancellations	(53)	(862)
Excess tax benefit related to stock options exercised	(1,772)	(14)
Other	(656)	1,352
Changes in assets and liabilities:		
Accounts receivable	5,083	6,248
Other receivables	12,467	16,722
Inventories	(4,586)	(5,381)
Prepaid expenses	2,014	(1,776)
Other assets	940	5,482
Accounts payable	(2,298)	(6,047)
Income taxes payable	(8,950)	16,918
Termination of derivative financial instrument	(7,376)	(3,250)
Other accrued expenses	(7,051)	2,144
Cash provided by operating activities	76,147	104,075
Cash flows from investing activities:		
Additions to property and equipment	(17,865)	(17,084)
Sales of available-for-sale securities		1,000
Cash used in investing activities	(17,865)	(16,084)
Cash flows from financing activities:		
Deemed landlord financing proceeds	1,635	2,567
Deemed landlord financing payments	(752)	(705)
Proceeds from exercise of employee stock options	11,587	350
Excess tax benefit related to stock options exercised	1,772	14
Repayment on credit facility	(30,000)	(75,000)
Purchase of treasury stock	(29,946)	
Cash used in financing activities	(45,704)	(72,774)
Net change in cash and cash equivalents	12,578	15,217
Cash and cash equivalents at beginning of period	73,715	80,365
Cash and cash equivalents at end of period	$ 86,293	$ 95,582
Supplemental disclosures:		
Interest paid	$ 14,281	$ 12,137

Income taxes paid	$	18,318	$	4,121

See the accompanying notes to the consolidated financial statements.

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THE CHEESECAKE FACTORY INCORPORATED AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Basis of Presentation and Significant Accounting Policies

The accompanying consolidated financial statements include the accounts of The Cheesecake Factory Incorporated (referred to herein as the Company, we, us and our) and its wholly owned subsidiaries prepared in accordance with accounting principles generally accepted in the Unite States of America (GAAP) and with the instructions to Form 10-Q and Article 10 of Regulation S-X. The financial statements presented herein have not been audited by an independent registered public accounting firm, but include all material adjustments (consisting of normal recurring adjustments) which are, in the opinion of management, necessary for the fair statement of the financial condition, results of operations and cash flows for the period. However, these results are not necessarily indicative of results for any other interim period or for the full fiscal year. The preparation of financial statements in conformity with GAAP requires us to make certain estimates and assumptions for the reporting periods covered by the financial statements. These estimates and assumptions affect the reported amounts of assets, liabilities, revenues and expenses and the disclosure of contingent liabilities. Actual amounts could differ from these estimates.

Certain information and footnote disclosures normally included in financial statements in accordance with GAAP have been omitted pursuant to the rules of the Securities and Exchange Commission (SEC). The accompanying consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto included in our Annual Report on Form 10-K for the fiscal year ended December 29, 2009 filed with the SEC on February 26, 2010.

Certain reclassifications have been made to prior year amounts to conform to the current year presentation.

Fair Value of Financial Instruments

For cash and cash equivalents, the carrying amount approximates fair value because of the short maturity of these instruments. The fair value of our long-term debt and deemed landlord financing liabilities are determined using current applicable rates for similar instruments as of the balance sheet date. During the second quarter of fiscal 2010, we performed a review of market conditions and the borrowing rates currently available to us for facilities with similar terms and maturities. Based on this analysis, we believe the carrying value of our long-term debt approximates fair value. The fair value of our deemed landlord financing liabilities is $51.0 million versus a carrying value of $52.6 million.

Recent Accounting Pronouncements

In October 2009, the Financial Accounting Standards Board issued guidance on revenue arrangements with multiple deliverables effective for us in fiscal 2011, although early adoption is permitted. The guidance revises the criteria for measuring and allocating consideration to each component of a multiple element arrangement. The guidance requires companies to allocate revenue using the relative selling price of each deliverable, which must be estimated if the company does not have either a history of selling the deliverable on a stand alone basis or third-party evidence of selling price. For our company, this guidance will only impact the pattern of revenue recognition for our marketing programs that include multiple elements. As the timing and content of future promotions is not determinable at this time, we are unable to estimate the impact of this guidance on our financial statements.

2. Inventories

Inventories consisted of (in thousands):

	June 29, 2010	December 29, 2009
Restaurant food and supplies	$ 12,194	$ 12,619
Bakery finished goods	10,123	5,530
Bakery raw materials and supplies	4,471	4,053
Total	$ 26,788	$ 22,202

3. Long-Term Debt

Long-term debt consisted of (in thousands):

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	June 29, 2010	December 29, 2009
Credit facility	$ 70,000	$ 100,000

In April 2007, we entered into a five-year revolving credit facility (Facility) with a maximum available borrowing commitment of $200 million. In March 2008, we amended the Facility to increase the maximum available borrowing commitment to $300 million. In January 2009, we entered into a second amendment, which reset our financial covenants and pricing, and also limited cash distributions with respect to our equity interests, such as cash dividends and share repurchases, based on a liquidity threshold. Borrowings under the amended Facility bear interest at a floating rate based on the London Interbank Offering Rate (LIBOR) plus a spread ranging from 2.50% to 2.75%, depending on our ratio of debt to trailing 12-month earnings before interest, taxes, depreciation, amortization and noncash stock option expense (EBITDA), as defined in the agreement. In addition, we pay a commitment fee ranging from 0.40% to 0.45%, also depending on our ratio of debt to EBITDA, calculated on the average unused portion of the Facility. The Facility restricts unsecured borrowings to $15 million and includes a pledge of our outstanding equity interests in The Cheesecake Factory Bakery Incorporated and The Cheesecake Factory Assets Co. LLC, which had carrying values of $85.8 million and $65.3 million, respectively, at June 29, 2010.

We are obligated to maintain certain financial covenants, which include a maximum debt to EBITDA ratio of 1.75 as of the fiscal quarter ending March 31, 2009 or 1.50 as of the end of any fiscal quarter thereafter, as well as a minimum EBITDAR (EBITDA plus rental expense), as defined in the Facility, to interest and rental expense ratio of 1.90 as of any of the fiscal quarters ending March 31, 2009 through September 28, 2010 or 2.00 as of the end of any fiscal quarter thereafter. At June 29, 2010, our EBITDA and EBITDAR ratios were 0.34 and 2.41, respectively. Therefore, we were in compliance with the financial covenants in effect under the Facility at that date.

Availability under the Facility is reduced by outstanding standby letters of credit, which are used to support our self-insurance programs. As of June 29, 2010, we had net availability for borrowings of $214 million, based on outstanding debt of $70 million and $16 million in standby letters of credit. Since we have the contractual ability to maintain the outstanding balance on our Facility, the debt is classified as long-term on our consolidated balance sheets.

4. Derivative Financial Instruments

At December 29, 2009, we held one zero-cost interest rate collar that hedged interest rate variability on the $100 million outstanding balance on our Facility as of that date. This instrument consisted of a combination of a purchased cap option with a three-month LIBOR cap rate of 5.35% and a sold floor option with a three-month LIBOR floor rate of 4.69%, and had a maturity date of April 3, 2012. During the second quarter of fiscal 2010, we unwound this collar at a cost of $7.4 million. See Note 3 for further discussion of our credit facility.

This derivative qualified for hedge accounting as a cash flow hedge and, accordingly, was recognized at fair value as either an asset or liability on the consolidated balance sheets. Changes in fair value were recorded in accumulated other comprehensive income (AOCI) and subsequently reclassified into earnings when the related interest expense on the underlying borrowing was recognized. We do not hold any derivative financial instruments for trading or speculative purposes.

The fair value and balance sheet locations of our derivative are as follows (in thousands):

	Balance Sheet Location	Fair Value of Liability Derivatives June 29, 2010	Fair Value of Liability Derivatives December 29, 2009
Interest rate contracts	Other accrued expenses	$	$ 4,299
Interest rate contracts	Other noncurrent liabilities		3,945
Total		$	$ 8,244

We had no derivative financial instruments in asset positions as of June 29, 2010 or December 29, 2009. The fair value of our derivative financial instruments is estimated using the net present value of a series of cash flows on both the cap and floor components of the interest rate collars. These cash flows are based on yield curves which take into account the contractual terms of the derivatives, including the period to maturity and market-based parameters such as interest rates and volatility. We incorporated nonperformance risk by adjusting the present value of each liability position utilizing an estimation of our credit risk.

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The effects of derivative instruments on our consolidated statements of operations are as follows (in thousands):

	Gain/(Loss) Recognized in AOCI on Derivative Thirteen Weeks Ended		Location of Gain/(Loss) Reclassified from AOCI into Income	Gain/(Loss) Reclassified from AOCI into Income Thirteen Weeks Ended	
	June 29, 2010	June 30, 2009		June 29, 2010	June 30, 2009
Interest rate contracts	$ (63)	$ 2,967	Interest expense	$ (8,498)	$ (4,453)

	Gain/(Loss) Recognized in AOCI on Derivative Twenty-Six Weeks Ended		Location of Gain/(Loss) Reclassified from AOCI into Income	Gain/(Loss) Reclassified from AOCI into Income Twenty-Six Weeks Ended	
	June 29, 2010	June 30, 2009		June 29, 2010	June 30, 2009
Interest rate contracts	$ 41	$ 2,764	Interest expense	$ (9,638)	$ (5,502)

5. Fair Value Measurement

The following table presents our financial assets and liabilities that were accounted for at fair value as of June 29, 2010 (in thousands):

	Fair Value Measurements Using		
	Quoted Prices in Active Markets	Significant Other Observable Inputs	Significant Unobservable Inputs
Assets:			