ABX AIR INC
Form 10-Q
May 09, 2007
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF

THE SECURITIES EXCHANGE ACT OF 1934

For Quarter Ended March 31, 2007

Commission File Number 000-50368

ABX AIR, INC.

(Exact name of registrant as specified in its charter)

Delaware **(State of incorporation or organization)**	**91-1091619** **(IRS Employer Identification No.)**

145 Hunter Drive

Wilmington, Ohio 45177

(Address of Principal Executive Office)

(937) 382-5591

(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. x Yes ¨ No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definitions of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer ¨ Accelerated filer x Non-accelerated filer ¨

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

As of May 9, 2007, ABX Air, Inc. had outstanding 58,678,437 shares of common stock, par value $.01.

ABX AIR, INC. AND SUBSIDIARIES

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FORWARD LOOKING STATEMENTS

Statements contained in this quarterly report on Form 10-Q that are not historical facts are considered forward-looking statements (as that term is defined in the Private Securities Litigation Reform Act of 1995). Words such as projects, believes, anticipates, will, estimates, plans, ex intends and similar words and expressions are intended to identify forward-looking statements. These forward-looking statements are based on expectations, estimates and projections as of the date of this filing, and involve risks and uncertainties that are inherently difficult to predict. Actual results may differ materially from those expressed in the forward-looking statements for any number of reasons, including those described in this report and in our 2006 Annual Report filed on Form 10-K with the Securities and Exchange Commission.

Filings with the Securities and Exchange Commission

Our filings with the Securities and Exchange Commission, including annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K, are available free of charge from our website at www.ABXAir.com as soon as reasonably practicable after filing with the SEC.

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PART 1. FINANCIAL INFORMATION

Item 1. Financial Statements

ABX AIR, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF EARNINGS

(In thousands, except share data)

	Three Months Ended March 31	
	2007	**2006**
REVENUES	$ 288,062	$ 369,165
OPERATING EXPENSES		
Salaries, wages and benefits	157,925	164,765
Fuel	58,953	61,338
Maintenance, materials and repairs	22,872	32,638
Depreciation and amortization	11,943	11,003
Landing and ramp	9,801	7,606
Rent	2,518	2,430
Purchased line-haul and yard management	1,671	65,494
Other	13,592	14,109
	279,275	359,383
INTEREST EXPENSE	(3,163)	(2,833)
INTEREST INCOME	1,258	1,144
EARNINGS BEFORE INCOME TAXES	6,882	8,093
INCOME TAX EXPENSE	(2,615)	
NET EARNINGS	$ 4,267	$ 8,093
EARNINGS PER SHARE		
Basic	$ 0.07	$ 0.14
Diluted	$ 0.07	$ 0.14
WEIGHTED AVERAGE SHARES		
Basic	58,282	58,270
Diluted	58,589	58,413

See notes to consolidated financial statements.

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ABX AIR, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(In thousands, except share data)

	March 31, 2007	December 31, 2006
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	$ 37,382	$ 63,219
Marketable securities available-for-sale	17,295	15,374
Accounts receivable, net of allowance of $516 in 2007 and 2006	17,060	10,365
Inventory	13,386	13,907
Prepaid supplies and other	5,764	6,395
Deferred income taxes	14,691	14,691
Aircraft and engines held for sale	2,079	2,219
TOTAL CURRENT ASSETS	107,657	126,170
Other assets	9,875	7,966
Deferred income taxes	82,070	87,024
Property and equipment, net	482,413	458,638
TOTAL ASSETS	$ 682,015	$ 679,798
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Accounts payable	$ 52,596	$ 65,313
Salaries, wages and benefits	42,146	53,173
Accrued expenses	9,753	10,298
Current portion of long-term obligations	12,557	11,413
Unearned revenue	9,087	4,081
TOTAL CURRENT LIABILITIES	126,139	144,278
Long-term obligations	202,712	189,118
Post-retirement liabilities	223,657	222,587
Other liabilities	4,028	3,605
Commitments and contingencies (Note G)		
STOCKHOLDERS' EQUITY:		
Preferred stock, 20,000,000 shares authorized, including 75,000 Series A Junior Participating Preferred Stock		
Common stock, par value $0.01 per share; 75,000,000 shares authorized; 58,678,437 and 58,539,300 shares issued and outstanding in 2007 and 2006, respectively	587	585
Additional paid-in capital	431,661	431,071
Accumulated deficit	(204,863)	(207,836)
Accumulated other comprehensive loss	(101,906)	(103,610)
TOTAL STOCKHOLDERS' EQUITY	125,479	120,210
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 682,015	$ 679,798

See notes to consolidated financial statements.

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ABX AIR, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

	Three Months Ended March 31	
	2007	**2006**
OPERATING ACTIVITIES:		
Net earnings	$ 4,267	$ 8,093
Adjustments to reconcile net earnings to net cash provided by operating activities:		
Depreciation and amortization	11,943	11,003
Pension and post-retirement amortization	2,854	
Deferred income taxes	2,615	
Stock-based compensation	592	258
Changes in assets and liabilities:		
Accounts receivable	(6,695)	6,665
Inventory and prepaid supplies	674	(1,601)
Accounts payable	(33,006)	(24,590)
Unearned revenue	5,205	4,265
Accrued expenses, salaries, wages and benefits and other liabilities	(11,348)	(5,467)
Post-retirement liabilities	1,070	8,212
Other	2	237
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	(21,827)	7,075
INVESTING ACTIVITIES:		
Capital expenditures	(14,738)	(12,952)
Proceeds from the sale of property and equipment	140	
Restricted deposits of interest-bearing funds	(4,745)	
Proceeds from redemptions of marketable securities	4,295	1,950
Purchases of marketable securities	(3,693)	(2,075)
NET CASH USED IN INVESTING ACTIVITIES	(18,741)	(13,077)
FINANCING ACTIVITIES:		
Principal payments on long-term obligations	(2,762)	(2,086)
Proceeds from borrowings on long-term obligations	17,500	
Financing fees	(7)	(23)
NET CASH PROVIDED (USED) IN FINANCING ACTIVITIES	14,731	(2,109)
NET DECREASE IN CASH	(25,837)	(8,111)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	63,219	69,473
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 37,382	$ 61,362
SUPPLEMENTAL CASH FLOW INFORMATION:		
Interest paid, net of amount capitalized	$ 1,471	$ 1,570
Income taxes paid	$	$

SUPPLEMENTAL NON-CASH INFORMATION:		
Accrued aircraft modification expenditures	$ 20,289	$ 10,024

See notes to consolidated financial statements.

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ABX AIR, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

March 31, 2007

NOTE A SUMMARY OF FINANCIAL STATEMENT PREPARATION AND SIGNIFICANT ACCOUNTING POLICIES

The interim period consolidated financial statements of ABX Air, Inc. and its subsidiaries (ABX or the Company) have been prepared in accordance with accounting principles generally accepted in the United States of America and rules and regulations of the Securities and Exchange Commission for interim financial information. Accordingly, they do not include all of the information, footnotes and disclosures required by generally accepted accounting principles for complete financial statements and are unaudited. The results of operations and cash flows for any interim periods are not necessarily indicative of results that may be reported for the full year. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. The December 31, 2006 financial amounts are extracted from the annual audited financial statements. The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. Intercompany balances and transactions between the Company and its subsidiaries are eliminated upon consolidation.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect amounts reported in the consolidated financial statements. Estimates and assumptions are used to record allowances for uncollectible amounts, self-insurance reserves, spare parts inventory, depreciation and impairments of property and equipment, labor contract settlements, post-retirement obligations, income taxes, contingencies and litigation. Changes in these estimates and assumptions may have a material impact on the consolidated financial statements.

Consolidation

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries. Intercompany balances and transactions are eliminated.

Revenue Recognition

The Company derives approximately 95% of its revenues from an aircraft, crew, maintenance and insurance agreement (ACMI agreement) and a hub services agreement (Hub Services agreement) with DHL Express (USA), Inc. (DHL). Revenues from DHL are determined based on the expenses incurred during a period and recognized when the related services are performed. Expenses incurred under these agreements are generally subject to a base mark-up of 1.75%, which is recognized in the period the expenses are incurred. Certain costs, the most significant of which include fuel, interest on a promissory note due to DHL, airport rent, ramp and landing fees, incurred under the two commercial agreements are reimbursed and included in revenues without mark-up. Beginning April 1, 2006, no mark-up was recorded on the over-the-road truck line-haul network while those operations were transitioned to DHL. Beginning May 1, 2006, the Company no longer operated the line-haul network for DHL.

Both agreements also allow the Company to earn incremental mark-up above the base 1.75% mark-up (up to 1.60% under the ACMI agreement and 2.10% under the Hub Services agreement), as determined from the achievement of certain cost-related and service goals outlined in the two commercial agreements. The agreements stipulate the setting of quarterly and annual cost-related goals and annual service goals specified in each of the two agreements. At the end of each quarter, the Company measures the achievement of quarterly goals and records any incremental revenues earned by achieving the goals during the quarter. In a similar way, the Company measures annual goals and records incremental revenues at the end of its fiscal year.

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The Company derives a portion of its revenues from customers other than DHL. Charter segment revenues are recognized on scheduled and non-scheduled flights when the specific flight has been completed. Aircraft parts and fuel sales are recognized when the parts and fuel are delivered. Revenues earned and expenses incurred in providing aircraft-related maintenance, repair and technical services are recognized in the period in which the services are completed and delivered to the customer. Revenues derived from transporting freight and sorting parcels are recognized upon delivery of shipments and completion of service.

Cash and Cash Equivalents

The Company classifies short-term, highly liquid investments with original maturities of three months or less as cash and cash equivalents. These investments are recorded at cost, which approximates fair value.

Inventory

The Company s inventory is comprised primarily of expendable spare parts and supplies used for internal consumption. These items are generally charged to expense when issued for use. The Company values aircraft spare parts inventory at weighted-average cost and maintains a related obsolescence reserve. The Company records an obsolescence reserve on a base stock of inventory for each fleet type. Inventory amortization for the obsolescence reserve corresponds to the expected life of each fleet type. Additionally, the Company monitors the usage rates of inventory parts and segregates parts that are technologically outdated or no longer used in its fleet types. Slow moving and segregated items are actively marketed and written down to their estimated net realizable values based on market conditions.

Management analyzes the inventory reserve for reasonableness at the end of each calendar quarter. That analysis includes consideration of the expected fleet life, amounts expected to be on hand at the end of a fleet life, and recent events and conditions that may impact the usability or value of inventory. Events or conditions that may impact the expected life, usability or net realizable value of inventory include additional aircraft maintenance directives from the Federal Aviation Administration, changes in Department of Transportation regulations, new environmental laws and technological advances.

Income Taxes

Income taxes have been computed using the asset and liability method, under which deferred income taxes are provided for the temporary differences between the financial reporting basis and the tax basis of the Company s assets and liabilities. Deferred taxes are measured using provisions of currently enacted tax laws. A valuation allowance against deferred tax assets is recorded when it is more likely than not that such assets will not be fully realized. Tax credits are accounted for as a reduction of income taxes in the year in which the credit originates.

Comprehensive Income (Loss)

Comprehensive income includes net income and other comprehensive income or loss. Other comprehensive income or loss results from changes in the Company s pension liability, unrealized gains and losses on available-for-sale marketable securities and gains and losses associated with interest rate hedging instruments.

Marketable Securities

Marketable securities classified as available-for-sale are recorded at their estimated fair market values and any unrealized gains and losses are included in accumulated other comprehensive income or loss within stockholders equity. Interest on marketable securities is included in interest income. Realized gains and losses of any securities sold are based on the specific identification method.

Property and Equipment

Property and equipment are stated at cost, net of any impairment recorded. The cost and accumulated depreciation of disposed property and equipment are removed from the accounts with any related gain or loss reflected in earnings from operations.

The Company periodically evaluates, when events or circumstances require, the useful lives, salvage values and fair values of property and equipment. The acceleration of depreciation expense or the recording of significant impairment losses could result from changes in the estimated useful lives of assets due to a number of reasons, such as an assessment done quarterly to determine if excess capacity exists in the air or ground networks or changes in regulations governing the use of aircraft.

Long-lived assets are reviewed for impairment when circumstances indicate the carrying value of an asset may not be recoverable. For assets that are to be held and used, impairment is recognized when the estimated undiscounted cash flows associated with the asset or group of assets are less than their carrying value. If an impairment exists, an adjustment is made to write the asset down to its fair value, and a loss is recorded as the difference between the carrying value and fair value. Fair values are determined based on quoted market values, discounted cash flows or internal and external appraisals, as applicable. Assets held for sale or disposition are carried at the lower of carrying value or fair value less the cost to sell.

The cost of modifying passenger aircraft to freighter aircraft configuration is capitalized as incurred. Interest costs incurred while aircraft are being modified are capitalized as an additional cost of the aircraft until the date the asset is placed in service. Capitalized interest was $0.4 million and $0.2 million for the quarters ended March 31, 2007 and 2006, respectively.

The cost of major airframe and engine overhauls on the Company s in-service fleet, as well as routine maintenance and repairs, are charged to expense as incurred.

Unearned Revenue

As specified in the two commercial agreements with DHL, the Company is advanced funds on each Monday for the costs budgeted to be incurred for the upcoming week. Unearned revenue reflects those funds that the Company has received in advance of incurring the associated cost to perform under the commercial agreements. Unearned revenue also includes advance payments from customers other than DHL.

Stock-Based Payments

The Company measures the cost of services received in exchange for stock-based awards using the grant-date fair value of the award. The cost of the awards is recognized over the period during which service is required to be provided. Restricted stock awards granted to employees vest over a service period. The restrictions on the non-vested restricted stock awards lapse at the end of a specified service period, which is approximately three years from the date of grant. Restrictions could lapse sooner upon a business combination, death, disability or after an employee qualifies for retirement.

Recent Accounting Pronouncements

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standard No. 157, Fair Value Measurements, (SFAS 157) which defines fair value, establishes a framework for measuring fair value and expands disclosure about fair value measurements. SFAS 157 will be effective for the Company s fiscal year beginning January 1, 2008. The Company has not yet evaluated the impact that SFAS 157 will have on its disclosures.

In February 2007, the FASB issued SFAS 159, The Fair Value Option for Financial Assets and Financial Liabilities Including an Amendment of SFAS 115, which allows for the option to measure financial instruments and certain other items at fair value. Unrealized gains and losses on items for which the fair value option has been elected are reported in earnings. Other than marketable securities and derivative instruments already measured at fair value, the Company does not presently have any financial assets or liabilities that it would elect to measure at fair value, and, therefore, the Company expects this standard will have no impact on its financial statements. SFAS 159 will be effective for the Company s fiscal year beginning January 1, 2008.

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NOTE B TRANSACTIONS WITH DHL

The Company s revenues, cash flows and liquidity resources are highly dependent on DHL. Substantially all of the Company s revenues are derived through contracted services provided to DHL. Revenues from contracted services performed for DHL were $273.0 million and $360.8 million for the quarter ended March 31, 2007 and 2006, respectively.

The Company s balance sheets include the following balances related to revenue transactions with DHL (in thousands):

Assets (Liabilities):	March 31, 2007	December 31, 2006
Accounts receivable	$ 11,719	$ 2,680
Accounts payable	(1,530)	(392)
Unearned revenue	(5,919)	(2,607)
Net asset (liability)	$ 4,270	$ (319)

The ACMI agreement has a term of seven years, expiring in August 2010. The Hub Services agreement has a term of four years, expiring in August 2007, with an automatic annual renewal, unless a ninety-day notice of non-renewal is given. The Company expects that the agreement will automatically renew in 2007 for a one-year period.

NOTE C MARKETABLE SECURITIES

The marketable securities held by the Company consist of debt securities, which are classified as available-for-sale. Marketable securities of approximately $2.9 million and $5.4 million as of March 31, 2007 and December 31, 2006, respectively, contractually mature after one year and are included in other assets within the Company s consolidated balance sheets. Expected maturities may differ from contractual maturities because the issuers of certain securities may have the right to prepay the obligations without prepayment penalties.

The following is a summary of the Company s marketable securities (in thousands):

	Estimated Fair Market Value	
	March 31, 2007	December 31, 2006
Obligations of U.S. Government Agencies	$ 6,348	$ 9,480
Obligations of U.S. corporations	13,895	11,336
Total marketable securities	$ 20,243	$ 20,816