

EXPEDITORS INTERNATIONAL OF WASHINGTON INC

Form 10-Q

November 05, 2015

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 September 30, 2015

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: 0-13468

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.

(Exact name of registrant as specified in its charter)

Washington

(State or other jurisdiction of
incorporation or organization)

91-1069248

(IRS Employer
Identification Number)

1015 Third Avenue, 12th Floor, Seattle, Washington

(Address of principal executive offices)

(206) 674-3400

(Registrant's telephone number, including area code)

98104

(Zip 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. (Check one):

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 ☒

At November 2, 2015, the number of shares outstanding of the issuer's Common Stock was 186,413,350.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.
AND SUBSIDIARIES

Condensed Consolidated Balance Sheets

(In thousands, except share data)

(Unaudited)

	September 30, 2015	December 31, 2014
Current Assets:		
Cash and cash equivalents	\$968,683	\$927,107
Short-term investments	8,260	40,336
Accounts receivable, less allowance for doubtful accounts of \$7,309 at September 30, 2015 and \$7,119 at December 31, 2014	1,166,300	1,236,042
Deferred Federal and state income taxes	20,862	20,279
Other	71,355	65,486
Total current assets	2,235,460	2,289,250
Property and equipment, less accumulated depreciation and amortization of \$379,996 at September 30, 2015 and \$371,756 at December 31, 2014	527,893	538,415
Goodwill	7,927	7,927
Other assets, net	55,738	55,313
Total assets	\$2,827,018	\$2,890,905
Current Liabilities:		
Accounts payable	718,555	770,238
Accrued expenses, primarily salaries and related costs	208,771	192,468
Federal, state and foreign income taxes	27,876	21,077
Total current liabilities	955,202	983,783
Deferred Federal and state income taxes	29,624	35,514
Commitments and contingencies		
Shareholders' Equity:		
Preferred stock, none issued	—	—
Common stock, par value \$0.01 per share. Issued and outstanding 186,183,201 shares at September 30, 2015 and 191,655,690 shares at December 31, 2014	1,862	1,916
Additional paid-in capital	874	1,113
Retained earnings	1,910,388	1,903,196
Accumulated other comprehensive loss	(74,079)	(37,817)
Total shareholders' equity	1,839,045	1,868,408
Noncontrolling interest	3,147	3,200
Total equity	1,842,192	1,871,608
Total liabilities and equity	\$2,827,018	\$2,890,905
See accompanying notes to condensed consolidated financial statements.		

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.
AND SUBSIDIARIES

Condensed Consolidated Statements of Earnings

(In thousands, except share data)

(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2015	2014	2015	2014
Revenues:				
Airfreight services	\$659,607	\$686,434	\$2,060,863	\$2,000,829
Ocean freight and ocean services	559,976	600,483	1,702,465	1,606,145
Customs brokerage and other services	431,749	418,188	1,257,083	1,188,917
Total revenues	1,651,332	1,705,105	5,020,411	4,795,891
Operating Expenses:				
Airfreight services	464,161	516,969	1,484,150	1,503,064
Ocean freight and ocean services	416,075	475,460	1,294,887	1,266,551
Customs brokerage and other services	201,115	199,420	589,766	563,720
Salaries and related costs	295,566	272,548	861,509	789,257
Rent and occupancy costs	25,747	26,396	76,106	76,959
Depreciation and amortization	11,475	12,741	34,424	37,540
Selling and promotion	10,370	9,240	30,146	26,704
Other	34,930	33,200	105,931	95,319
Total operating expenses	1,459,439	1,545,974	4,476,919	4,359,114
Operating income	191,893	159,131	543,492	436,777
Other Income (Expense):				
Interest income	2,666	2,793	8,034	8,254
Other, net	(3,085)) 2,336	753	5,245
Other (expense) income, net	(419)) 5,129	8,787	13,499
Earnings before income taxes	191,474	164,260	552,279	450,276
Income tax expense	72,738	61,463	207,882	171,556
Net earnings	118,736	102,797	344,397	278,720
Less net earnings attributable to the noncontrolling interest	426	416	1,623	1,213
Net earnings attributable to shareholders	\$118,310	\$102,381	\$342,774	\$277,507
Diluted earnings attributable to shareholders per share	\$0.62	\$0.53	\$1.79	\$1.40
Basic earnings attributable to shareholders per share	\$0.63	\$0.53	\$1.80	\$1.41
Dividends declared and paid per common share	\$—	\$—	\$0.36	\$0.32
Weighted average diluted shares outstanding	189,641,774	195,001,267	191,447,796	197,953,810
Weighted average basic shares outstanding	188,424,400	194,419,071	190,231,986	197,305,251

See accompanying notes to condensed consolidated financial statements.

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.
AND SUBSIDIARIES

Condensed Consolidated Statements of Comprehensive Income

(In thousands)

(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2015	2014	2015	2014
Net earnings	\$118,736	\$102,797	\$344,397	\$278,720
Other comprehensive income (loss), net of tax:				
Foreign currency translation adjustments, net of tax of \$11,669 and \$9,954 for the three months ended September 30, 2015 and 2014 and \$19,866 and \$8,560 for the nine months ended September 30, 2015 and 2014	(21,692)	(18,351)	(37,081)	(15,743)
Reclassification adjustment for foreign currency realized losses, net of tax of \$61 for the nine months ended September 30, 2014	—	—	—	111
Other comprehensive loss	(21,692)	(18,351)	(37,081)	(15,632)
Comprehensive income	97,044	84,446	307,316	263,088
Less comprehensive income attributable to the noncontrolling interest	35	234	804	1,094
Comprehensive income attributable to shareholders	\$97,009	\$84,212	\$306,512	\$261,994
See accompanying notes to condensed consolidated financial statements.				

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.
AND SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows

(In thousands)

(Unaudited)

	Three months ended September 30,		Nine months ended September 30,	
	2015	2014	2015	2014
Operating Activities:				
Net earnings	\$ 118,736	\$ 102,797	\$ 344,397	\$ 278,720
Adjustments to reconcile net earnings to net cash from operating activities:				
Provision for losses (recoveries) on accounts receivable	134	564	995	(55)
Deferred income tax (benefit) expense	(7,611)	(2,085)	13,312	8,000
Excess tax benefits from stock plans	—	(47)	(1,846)	(1,031)
Stock compensation expense	10,919	10,049	32,489	32,220
Depreciation and amortization	11,475	12,741	34,424	37,540
Other	2	139	115	345
Changes in operating assets and liabilities:				
Decrease (increase) in accounts receivable	2,466	(58,984)	18,910	(131,374)
(Decrease) increase in accounts payable and accrued expenses	(19,622)	23,113	3,311	114,036
Increase (decrease) in income taxes payable, net	19,978	2,050	4,110	(27,115)
Increase in other current assets	(3,801)	(3,646)	(1,419)	(5,852)
Net cash from operating activities	132,676	86,691	448,798	305,434
Investing Activities:				
Purchase of short-term investments	—	(40,275)	(47,008)	(136,706)
Proceeds from maturities of short-term investments	38,788	86,107	79,084	122,726
Purchase of property and equipment	(9,546)	(8,255)	(31,903)	(26,650)
Escrow deposit for land acquisition	—	—	—	(27,101)
Other, net	(2,666)	370	(2,482)	504
Net cash from investing activities	26,576	37,947	(2,309)	(67,227)
Financing Activities:				
Proceeds from issuance of common stock	54,606	28,452	114,701	58,469
Repurchases of common stock	(209,970)	(117,044)	(415,475)	(475,160)
Excess tax benefits from stock plans	—	47	1,846	1,031
Dividends paid	—	—	(68,781)	(62,807)
Distributions to noncontrolling interest	—	—	(857)	(85)
Net cash from financing activities	(155,364)	(88,545)	(368,566)	(478,552)
Effect of exchange rate changes on cash and cash equivalents	(20,932)	(16,174)	(36,347)	(16,827)
(Decrease) increase in cash and cash equivalents	(17,044)	19,919	41,576	(257,172)
Cash and cash equivalents at beginning of period	985,727	970,561	927,107	1,247,652
Cash and cash equivalents at end of period	\$ 968,683	\$ 990,480	\$ 968,683	\$ 990,480
Taxes Paid:				
Income taxes	\$ 60,374	\$ 61,899	\$ 190,024	\$ 195,358

See accompanying notes to condensed consolidated financial statements.

EXPEDITORS INTERNATIONAL OF WASHINGTON, INC.
AND SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements

(In thousands, except share data)

(Unaudited)

Note 1. Summary of Significant Accounting Policies

A. Basis of Presentation

Expeditors International of Washington, Inc. (“the Company”) is a non-asset based provider of global logistics services operating through a worldwide network of offices and exclusive or non-exclusive agents. The Company’s customers include retailing and wholesaling, electronics, industrial and manufacturing companies around the world.

The condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. As a result, certain information and note disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States (U.S. GAAP) have been condensed or omitted. The Company believes that the disclosures made are adequate to make the information presented not misleading. The condensed consolidated financial statements reflect all adjustments, consisting of normal recurring items, which are, in the opinion of management, necessary to a fair statement of the results for the interim periods presented. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and related notes included in the Company's Form 10-K as filed with the Securities and Exchange Commission on February 26, 2015.

All significant intercompany accounts and transactions have been eliminated in consolidation. All dollar amounts in the notes are presented in thousands except for share data. Effective in the first quarter of 2015, the Company changed the organization of the management of its Asia Pacific region, splitting it into North and South Asia. Accordingly, the financial information previously combined under one geographical operating segment for Asia Pacific is now reported as North Asia and South Asia segments for all periods presented.

B. Accounts Receivable

The Company maintains an allowance for doubtful accounts, which is reviewed at least monthly for estimated losses resulting from the inability of its customers to make required payments for services and advances. Additional allowances may be necessary in the future if the ability of its customers to pay deteriorates. The Company has recorded an allowance for doubtful accounts in the amounts of \$7,309 as of September 30, 2015 and \$7,119 as of December 31, 2014. Additions and write-offs have not been significant in the periods presented.

C. Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of the assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the period. The Company uses estimates primarily in the following areas: accounts receivable valuation, accrual of costs related to ancillary services the Company provides, accrual of insurance liabilities for the portion of the related exposure which the Company has self-insured, accrual of various tax liabilities, accrual of loss contingencies and calculation of share-based compensation expense. Actual results could differ from those estimates.

D. Recent Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board (FASB) issued Accounting Standards Update (ASU) 2014-09 (Topic 606) “Revenue from Contracts with Customers”, as amended. This update, which supersedes the revenue recognition requirements in Accounting Standards Codification (ASC) Topic 605 - “Revenue Recognition” and most industry-specific guidance throughout the industry topics of the FASB ASC, substantially converges revenue recognition guidance between U.S. GAAP and International Financial Reporting Standards (IFRS), providing a single, comprehensive framework for recognizing revenue. ASU 2014-09 will be effective for the Company beginning in its first quarter of 2018. The Company is currently evaluating the impact of adopting ASU 2014-09 on its consolidated financial statements and related disclosures. However, at this time, based on the nature of the Company's operations, the adoption of ASU 2014-09 is not expected to have a material impact on the amount or timing of revenue

recognized or the Company's revenue recognition policies.

Note 2. Share-Based Compensation

The Company provides compensation benefits by granting stock options and employee stock purchase rights to its employees and restricted shares to its directors. On May 21, 2015, the shareholders approved the 2015 Stock Option Plan, which made available 3,000,000 shares of the Company's common stock for purchase upon exercise of options granted. The Company has historically granted the majority of its options during the second quarter of each fiscal year. For the nine months ended September 30, 2015 and 2014, 2,955,750 and 2,289,600 options were granted, respectively. The grant of employee stock purchase rights and the issuance of shares under the employee stock purchase plan are made in the third quarter of each fiscal year and 699,438 and 671,775 were issued in the nine-month periods ended September 30, 2015 and 2014, respectively. In the second quarter of 2015 and 2014, respectively, 33,848 and 30,702 fully vested shares were granted to independent directors.

The Company recognizes stock compensation expense based on an estimate of the fair value of awards granted to employees and directors under the Company's stock option, director restricted stock and employee stock purchase rights plans. The expense, adjusted for expected forfeitures, is recognized on a straight-line basis over the stock awards' vesting period. The forfeiture assumption used to calculate compensation expense is primarily based on historical pre-vesting employee forfeiture patterns.

The fair value of each option grant is estimated on the date of grant using the Black-Scholes option pricing model with the following assumptions:

	Nine months ended September 30,	
	2015	2014
Dividend yield	1.60 %	1.50 - 1.51%
Volatility - stock option plans	29 - 34%	36 %
Volatility - stock purchase rights plans	20 %	20 %
Risk free interest rates	0.30 - 2.04%	0.11 - 2.27%
Expected life (years) - stock option plans	6.41 - 7.47	6.52 - 7.43
Expected life (years) - stock purchase rights plans	1	1
Weighted average fair value of stock options granted during the period	\$13.44	\$14.08
Weighted average fair value of stock purchase rights granted during the period	\$10.45	\$9.60

Total stock compensation expense and the total related tax benefit recognized are as follows:

	Three months ended September 30,		Nine months ended September 30,	
	2015	2014	2015	2014
Stock compensation expense	\$10,919	\$10,049	\$32,489	\$32,220
Recognized tax benefit	\$1,571	\$988	\$4,305	\$3,115

Note 3. Basic and Diluted Earnings per Share

The following table reconciles the numerator and the denominator of the basic and diluted per share computations for earnings attributable to shareholders:

(Amounts in thousands, except share and per share amounts)	Three months ended September 30,		
	Net earnings attributable to shareholders	Weighted average shares	Earnings per share
2015			
Basic earnings attributable to shareholders	\$ 118,310	188,424,400	\$ 0.63
Effect of dilutive potential common shares	—	1,217,374	—
Diluted earnings attributable to shareholders	\$ 118,310	189,641,774	\$ 0.62
2014			
Basic earnings attributable to shareholders	\$ 102,381	194,419,071	\$ 0.53
Effect of dilutive potential common shares	—	582,196	—
Diluted earnings attributable to shareholders	\$ 102,381	195,001,267	\$ 0.53

(Amounts in thousands, except share and per share amounts)	Nine months ended September 30,		
	Net earnings attributable to shareholders	Weighted average shares	Earnings per share
2015			
Basic earnings attributable to shareholders	\$ 342,774	190,231,986	\$ 1.80
Effect of dilutive potential common shares	—	1,215,810	—
Diluted earnings attributable to shareholders	\$ 342,774	191,447,796	\$ 1.79
2014			
Basic earnings attributable to shareholders	\$ 277,507	197,305,251	\$ 1.41
Effect of dilutive potential common shares	—	648,559	—
Diluted earnings attributable to shareholders	\$ 277,507	197,953,810	\$ 1.40

The following potential common shares have been excluded from the computation of diluted earnings per share because the effect would have been antidilutive:

	Three months ended September 30,		Nine months ended September 30,	
	2015	2014	2015	2014
Shares	8,379,877	14,886,109	9,713,102	16,532,462

Note 4. Components of Equity

The components of equity for the nine months ended September 30, 2015 and 2014 are as follows:

	Shareholders' equity	Noncontrolling interest	Total equity
Balance at December 31, 2014	\$ 1,868,408	3,200	1,871,608
Exercise of stock options	88,851	—	88,851
Issuance of shares under stock purchase plan	25,850	—	25,850
Shares repurchased under provisions of stock repurchase plans	(415,475)	—	(415,475)
Stock compensation expense	32,489	—	32,489
Tax benefits from stock plans, net	1,191		