APPLICA INC
Form 10-Q
April 29, 2005

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UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

þ **QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED MARCH 31, 2005**

OR

o **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 1-10177

APPLICA INCORPORATED

(Exact Name of Registrant as Specified in its Charter)

Florida	**59-1028301**
(State or Other Jurisdiction of Incorporation or Organization)	(I.R.S. Employer Identification Number)
3633 Flamingo Road, Miramar, Florida	**33027**
(Address Of Principal Executive Offices)	(Zip Code)

(954) 883-1000

(Registrant s Telephone Number, Including Area Code)

Former Name, If Changed Since Last Report:
Not Applicable

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 requirement for the past 90 days. Yes þ No o

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes þ No o

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date:

Class	Number of shares outstanding on April 25, 2005
Common Stock, $0.10 par value	24,136,591

APPLICA INCORPORATED

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PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

Applica Incorporated and Subsidiaries

CONSOLIDATED BALANCE SHEETS
(In thousands, except par value data)

	March 31, 2005 (Unaudited)	December 31, 2004
Assets		
Current Assets:		
Cash and cash equivalents	$ 6,204	$ 10,463
Accounts and other receivables, less allowances of $10,627 in 2005 and $11,711 in 2004	100,865	160,436
Notes receivable former officer	1,072	2,569
Inventories	113,199	131,503
Prepaid expenses and other	7,271	12,309
Refundable income taxes	2,696	2,032
Future income tax benefits	2,194	33
Total current assets	233,501	319,345
Property, Plant and Equipment - at cost, less accumulated depreciation of $69,410 in 2005 and $73,171 in 2004	35,973	38,327
Future Income Tax Benefits, Non-Current	9,762	11,212
Other Intangibles, Net	4,015	4,493
Other Assets	2,763	2,560
Total Assets	$ 286,014	$ 375,937
Liabilities and Shareholders Equity		
Current Liabilities:		
Accounts payable	$ 26,697	$ 41,827
Accrued expenses	46,184	62,046
Short-term debt	57,491	89,455
Current portion of long-term debt	3,000	3,000
Current taxes payable	2,286	5,947
Deferred rent	695	680
Total current liabilities	136,353	202,955
Other Long-Term Liabilities	933	1,004
Long-Term Debt	60,404	61,008
Shareholders Equity:		

Common stock authorized: 75,000 shares of $0.10 par value; issued and outstanding: 24,137 shares in 2005 and 2004		2,414		2,414
Paid-in capital		159,131		159,131
Accumulated deficit		(69,435)		(46,480)
Note receivable former officer		(502)		(502)
Accumulated other comprehensive loss		(3,284)		(3,593)
Total shareholders equity		88,324		110,970
Total Liabilities and Shareholders Equity	$	286,014	$	375,937

The accompanying notes are an integral part of these financial statements.

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Applica Incorporated and Subsidiaries

CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)

	Three Months Ended March 31,			
	2005		2004	
	(In thousands, except per share data)			
Net sales	$ 112,450	100.0%	$ 128,527	100.0%
Cost of goods sold	93,722	83.3	95,022	73.9
Gross profit	18,728	16.7	33,505	26.1
Selling, general and administrative expenses:				
Operating expenses	39,243	34.9	39,578	30.8
Restructuring and other credits			(563)	(0.4)
Operating loss	(20,515)	(18.2)	(5,510)	(4.3)
Other expense (income):				
Interest expense	2,441	2.2	2,115	1.6
Interest and other income	(275)	(0.2)	(347)	(0.3)
Loss on early extinguishment of debt			187	0.1
	2,166	1.9	1,955	1.5
Loss before income taxes	(22,681)	(20.2)	(7,465)	(5.8)
Income tax provision (benefit)	274	0.2	(2,986)	(2.3)
Net loss	$ (22,955)	(20.4)%	$ (4,479)	(3.5)%
Earnings (loss) per common share:				
Loss per common share basic and diluted	$ (0.95)		$ (0.19)	

The accompanying notes are an integral part of these financial statements.

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Applica Incorporated and Subsidiaries

CONSOLIDATED STATEMENTS OF CASH FLOWS (Unaudited)

	Three Months Ended March 31,	
	2005	2004
	(In thousands)	
Cash flows from operating activities:		
Net loss	$ (22,955)	$ (4,479)
Reconciliation to net cash provided by operating activities:		
Depreciation of property, plant and equipment	2,927	3,531
Loss on disposal of equipment	818	
(Recovery) provision for doubtful accounts	(515)	391
Write-downs of inventory	9,436	
Amortization of intangible and other assets	579	564
Loss on early extinguishment of debt		187
Deferred taxes	(711)	(3,026)
Restructuring credits		(563)
Changes in assets and liabilities:		
Accounts and other receivables	60,086	33,457
Inventories	8,379	(2,671)
Prepaid expenses and other	5,038	945
Other assets	5	(26)
Accounts payable and accrued expenses	(30,991)	(672)
Current income taxes	(4,325)	1,745
Other liabilities	(56)	6
Net cash provided by operating activities	27,715	29,389
Cash flows from investing activities:		
Additions to property, plant and equipment	(1,480)	(4,325)
Proceeds from sale of equipment	89	
Distributions from joint venture net		1,188
Receivable from former officer	1,504	(17)
Net cash provided by (used in) investing activities	113	(3,154)
Cash flows from financing activities:		
Net payments under lines of credit	(32,568)	(29,372)
Redemption of long-term debt		(4,390)
Exercise of stock options and issuance of common stock under employee stock purchase plan		799
Interest receivable from former officer	(7)	(5)
Net cash used in financing activities	(32,575)	(32,968)

Effect of exchange rate changes on cash	488	97
Decrease in cash and cash equivalents	(4,259)	(6,636)
Cash and cash equivalents at beginning of period	10,463	12,735
Cash and cash equivalents at end of period	$ 6,204	$ 6,099
Supplemental Disclosures of Cash Flow Information:		
Cash paid during the three-month period ended March 31:		
Interest	$ 3,807	$ 3,645
Income taxes	$ 4,599	

The accompanying notes are an integral part of these financial statements.

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Applica Incorporated and Subsidiaries

Notes to Consolidated Financial Statements

1. SUMMARY OF ACCOUNTING POLICIES
Interim Reporting

The accompanying unaudited consolidated financial statements include the accounts of Applica Incorporated and its subsidiaries (Applica). All significant intercompany transactions and balances have been eliminated. The unaudited consolidated financial statements have been prepared in conformity with Rule 10-01 of Regulation S-X of the Securities and Exchange Commission and therefore do not include information or footnotes necessary for a complete presentation of financial position, results of operations and cash flows in conformity with accounting principles generally accepted in the United States of America. However, all adjustments (consisting of normal recurring accruals), which, in the opinion of management, are necessary for a fair presentation of the financial statements, have been included. Operating results for the period ended March 31, 2005 are not necessarily indicative of the results that may be expected for the future fiscal quarters in 2005 or the full year ending December 31, 2005 due to seasonal fluctuations in Applica s business, changes in economic conditions and other factors. For further information, please refer to the Consolidated Financial Statements and Notes thereto contained in Applica s Annual Report on Form 10-K for the year ended December 31, 2004.

Reclassifications

Certain prior period amounts have been reclassified for comparability.

Cooperative Advertising and Slotting Fees

Effective January 1, 2005, Applica modified its accounting treatment for cooperative advertising and slotting fees it provides to its customers. The modification was necessitated by the fact that Applica will no longer use the services of an unrelated third party to verify performance and determine the fair value of the benefits Applica receives. In accordance with Emerging Issues Task Force (EITF) 01-9, Accounting for Consideration Given By a Vendor To a Customer (Including a Reseller of the Vendor s Products) , which addresses the income statement classification of slotting fees and cooperative advertising arrangements with trade customers. Given the change referred to above, these considerations should be accounted for as a reduction of selling price and netted against sales. Prior to January 1, 2005, Applica classified these considerations as selling, general and administrative expenses in its consolidated statement of operations. This modification reduced each of net sales, gross profit and selling, general and administrative expenses by $3.3 million and $4.0 million for the three months ending March 31, 2005 and 2004, respectively. Because the modification resulted solely in reclassification within the consolidated statement of operations, there was no impact on Applica s financial condition, operating income or net earnings for any of the periods presented.

Inventories

Inventories are stated at the lower of cost or market; cost is determined by the first-in, first-out method. Inventories are comprised of the following:

	March 31, 2005	December 31, 2004

	(In thousands)	
Raw materials	$ 6,217	$ 4,528
Work in process	199	280
Finished goods	106,783	126,695
	$ 113,199	$ 131,503

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Applica Incorporated
Notes to Consolidated Financial Statements Continued

Stock Based Compensation

At March 31, 2005, Applica had four active stock based compensation plans. Applica accounts for stock-based compensation using the intrinsic value method. Accordingly, compensation expense for stock options issued is measured as the excess, if any, of the fair value of Applica s common stock at the date of grant over the exercise price of the options. Applica s net earnings (loss) and earnings (loss) per share would have been changed to the pro forma amounts indicated below had compensation expense for the stock option plans and non-qualified options issued to employees been determined based on the fair value of the options at the grant dates consistent with the method of Statement of Financial Accounting Standards (SFAS) No. 123.

	For the Three Months Ended March 31,			
	2005		2004	
	(In thousands, except per share data)			
Net loss, as reported	$	(22,955)	$	(4,479)
Add: Stock-based employee compensation expense included in net loss				
Deduct: Total stock-based employee compensation expense determined under fair value based method		(304)		(102)
Pro forma net loss	$	(23,259)	$	(4,581)
Loss per share:				
Basic as reported	$	(0.95)	$	(0.19)
Basic pro forma	$	(0.96)	$	(0.19)
Diluted as reported	$	(0.95)	$	(0.19)
Diluted pro forma	$	(0.96)	$	(0.19)

The above pro forma disclosures may not be representative of the effects on reported net earnings (loss) for future periods as options vest over several years and Applica may continue to grant options to employees.

In accordance with the requirements of SFAS 123, the fair value of each option grant was estimated on the date of grant using a binomial option-pricing model with the following weighted-average assumptions:

	For the Three Months Ended March 31,	
	2005	2004
Expected dividend yield	00.0%	00.0%
Expected price volatility	24.2%	64.1% - 82.7%
Risk-free interest rate	3.15%	3.0%
Expected life of options in years	4	4

Comprehensive Loss

The components of other comprehensive loss, net of tax, were as follows:

	March 31, 2005	March 31, 2004
	(In thousands)	
Loss	$ (22,955)	$ (4,479)
Foreign currency translation adjustment	(295)	(200)
Change in market value of derivatives	604	106
	$ (22,646)	$ (4,573)

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Applica Incorporated
Notes to Consolidated Financial Statements Continued

Recent Accounting Pronouncements

In the fourth quarter of 2004, the FASB issued Statement No. 123 (revised 2004), or SFAS No. 123R, Share-Based Payment, which replaces Statement No. 123 Accounting for Stock-Based Compensation, and supersedes APB Opinion No. 25, Accounting for Stock Issued to Employees. SFAS No. 123R eliminates the alternative to use APB Opinion 25 s intrinsic value method of accounting that was provided in Statement No. 123 as originally issued. After a phase-in period for Statement No. 123R, pro forma disclosure will no longer be allowed. In the first quarter of 2005, the Securities and Exchange Commission (SEC) issued Staff Accounting Bulletin No. 107 which provided further clarification on the implementation of SFAS No. 123R.

Alternative phase-in methods are allowed under Statement No. 123R, which was to be effective as of the beginning of the first interim or annual reporting period that begins after June 15, 2005. The SEC announced in the second quarter of 2005 that it would extend this phase-in period and, therefore, Applica s effective date for implementation of SFAS 123R is January 1, 2006. Applica does not believe that any of the alternative phase-in methods would have a materially different effect on Applica s consolidated statement of operations or balance sheet.

2. SHAREHOLDERS EQUITY
Loss Per Share

Weighted average basic shares for the three-month periods ended March 31, 2005 and 2004 were 24,136,545 and 23,718,256, respectively.

The following table shows potential common stock equivalents outstanding to purchase shares of common stock that were excluded in the computation of diluted loss per share. All common stock equivalents have been excluded from the diluted per share calculations in the three-month periods ended March 31, 2005 and 2004, because their inclusion would have been anti-dilutive.

	For the Three Months Ended March 31,	
	2005	2004
Number of shares	2,616,617	2,337,128
Range of exercise price	$ 3.63-31.69	$ 3.63-31.69

3. COMMITMENTS AND CONTINGENCIES

Applica is subject to legal proceedings, product liability claims and other claims that arise in the ordinary course of our business. In the opinion of management, the amount of ultimate liability with respect to such matters, if any, in excess of applicable insurance coverage, is not likely to have a material effect on Applica s business, financial condition, results of operations or liquidity. However, as the outcome of litigation or other claims is difficult to predict, significant changes in the estimated exposures could occur.

4. COST OF GOODS SOLD

Included in cost of sales for the first quarter of 2005 are inventory write-downs of approximately $9.4 million related to lower-than-anticipated consumer demand for two of our products. Also, included in cost of sales for the three months ended March 31, 2005 are restructuring charges of $0.9 million related to our decision to move the production of Home Café single cup coffee maker from Mexico to third party manufacturers in China. The restructuring charges consist of $0.3 million in severance charges and $0.6 million in the acceleration of the depreciation of machinery and equipment used in the manufacturing process. Included in cost of sales for the three months ended March 31, 2004 are restructuring charges of $0.9 million primarily related to the downsizing of our Hong-Kong based manufacturing facilities. The Hong Kong based manufacturing operations were sold in July 2004.

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Applica Incorporated
Notes to Consolidated Financial Statements Continued

The inventory write-downs relate to the Household Products reportable segment. All restructuring charges relate to the Manufacturing reportable segment.

5. PROPERTY, PLANT AND EQUIPMENT

The following is a summary of property, plant and equipment:

	Useful Lives	March 31, 2005	December 31, 2004
		(Dollars in thousands)	
Building	20 years	$ 7,430	$ 7,430
Computer equipment	3 - 5 years	32,232	31,635
Equipment and other	3 - 8 years	61,253	66,985
Leasehold improvements*	8 - 10 years	3,399	4,379
Land and land improvements**	20 years	1,069	1,069
Total		105,383	111,498
Less accumulated depreciation		69,410	73,171
		$ 35,973	$ 38,327

* Shorter of remaining term of lease or useful life

** Only improvements are depreciated

At March 31, 2005, Applica completed the implementation of a major upgrade of its information technology infrastructure, including the installation of a new enterprise resource planning system. As of March 31, 2005 and December 31, 2004, approximately $12.4 million and $11.8 million, respectively, of capitalized expenditures associated with the information technology upgrade were included in property, plant and equipment as assets not yet placed in service.

6. RESTRUCTURING AND OTHER CHARGES

For the three months ended March 31, 2005, the activity relating to the accrued restructuring and other charges was as follows:

	Amount Accrued at Dec. 31,	2005	Amount Accrued at March 31,

	2004	Payments	2005
		(In thousands)	
Back-office consolidation	$ 2,536	$ (526)	$ 2,010

The amounts accrued in connection with the restructuring and other charges were reflected in accrued expenses in the accompanying consolidated balance sheets.

7. INTANGIBLE ASSETS

The components of Applica s intangible assets subject to amortization are as follows:

		March 31, 2005		December 31, 2004	
	Average Life (Years)	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
			(In thousands)		
Licenses	4.0	$ 3,000	$ (1,337)	$ 3,000	$ (1,055)
Contract-Based	6.4	5,988	(3,636)	5,988	(3,440)
		$ 8,988	$ (4,973)	$ 8,988	$ (4,495)

Applica Incorporated
Notes to Consolidated Financial Statements Continued

Amortization expense for intangible assets during the three months ended March 31, 2005 and 2004 was $0.5 million and $0.4 million, respectively.

8. PRODUCT WARRANTY OBLIGATIONS

Estimated future warranty obligations related to certain products are provided by charges to operations in the period in which the related revenue is recognized. Accrued product warranties as of March 31, 2005 and December 31, 2004 were as follows:

		(In thousands)
Balance at December 31, 2004	$	7,183
Additions to accrued product warranties		7,499
Reductions of accruals payments and credits issued		(10,371)
Balance at March 31, 2005	$	4,311

9. SHORT-TERM DEBT

Revolving Credit Facility

Applica has a revolving credit facility with a syndicate of banks that provides for borrowings on a revolving basis of up to $175 million with a $10 million sublimit for letters of credit (the credit facility). The credit facility has a maturity date of November 2009. Advances under the credit facility are governed by Applica s collateral value, which is based upon percentages of eligible accounts receivable and inventories. If Applica does not maintain a minimum fixed charge coverage ratio of 1.0 to 1.0, Applica must maintain a minimum daily availability under its borrowing base of $20 million and a minimum average daily availability of $30 million. If Applica maintains a fixed charge coverage ratio of greater than 1.0 to 1.0, but less than 2.0 to 1.0, there is no availability requirement, however there is an availability block of $10 million. If Applica maintains a fixed charge coverage ratio of greater than 2.0 to 1.0, there is no availability requirement and no availability block.

As of March 31, 2005, Applica s fixed charge coverage ratio was less than 1.0 to 1.0. During the three months ended March 31, 2005, Applica maintained daily availability greater than $20 million and average daily availability greater than $30 million.

As of March 31, 2005, Applica was borrowing approximately $57.1 million under the credit facility and had approximately $49.9 million of availability for future cash borrowings. Also, as March 31, 2005, Applica had letters of credit of $1.5 million outstanding under its credit facility.

At Applica s option, interest accrues on the loans made under the credit facility at either:

LIBOR (adjusted for any reserves), plus a specified margin (determined by Applica s Fixed Charge Coverage Ratio and set at 2.25% at March 31, 2005), which was 5.12% at March 31, 2005; or

the Base Rate (which is Bank of America s prime rate), plus a specified margin (determined based upon Applica s Fixed Charge Coverage Ratio and was zero at March 31, 2005), which was 5.75% at March 31, 2005.

Swing loans up to $15.0 million bear interest at the Base Rate plus a specified margin (determined based on Applica s leverage ratio and was zero at March 31, 2005), which was 5.75% at March 31, 2005.

The credit facility contains a number of significant covenants that, among other things, restrict the ability of Applica to dispose of assets, incur additional indebtedness, prepay other indebtedness, pay dividends, repurchase or redeem capital stock, enter into certain investments or create new subsidiaries, enter into sale and lease-back transactions, make certain acquisitions, engage in mergers or consolidations, create liens, or engage in certain transactions with affiliates, and that otherwise restrict corporate and business activities. As of March 31, 2005, Applica was in compliance with all covenants under the credit facility.

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Applica Incorporated
Notes to Consolidated Financial Statements Continued

Although the credit facility expires in November 2009, Applica has classified the borrowings thereunder as a current liability in accordance with Emerging Issues Task Force (EITF) 95-22 Balance Sheet Classifications of Borrowings Outstanding under Revolving Credit Agreements That Include Both a Subjective Acceleration Clause and a Lock-Box Arrangement.

Notes and Acceptance Payable

Certain of Applica s foreign subsidiaries have approximately $1.3 million in trade finance lines of credit, payable on demand, which are secured by the subsidiaries tangible and intangible property and a guarantee by the parent company, Applica Incorporated. As of March 31, 2005, there was $0.4 million outstanding under the working capital lines and $0.9 million outstanding under the letter of credit lines.

10. BUSINESS SEGMENTS

Applica currently manages its operations through three business segments: Household Products, Professional Personal Care Products and Manufacturing. Segment information for the three months ended March 31, 2005 and 2004 was as follows:

Professional