

LINCOLN ELECTRIC HOLDINGS INC

Form 10-Q

April 25, 2014

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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 March 31, 2014

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: 0-1402

LINCOLN ELECTRIC HOLDINGS, INC.

(Exact name of registrant as specified in its charter)

Ohio

34-1860551

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

22801 St. Clair Avenue, Cleveland, Ohio

44117

(Address of principal executive offices)

(Zip Code)

(216) 481-8100

(Registrant's telephone number, including area code)

Not applicable

(Former name, former address and former fiscal year, if changed since last report)

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 "small 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

The number of shares outstanding of the registrant's common shares as of March 31, 2014 was 80,425,365.

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EX-31.2 Certification of the Executive Vice President, Chief Financial Officer and Treasurer (Principal Financial Officer) pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934.	
EX-32.1 Certification of the Chairman, President and Chief Executive Officer (Principal Executive Officer) and Executive Vice President, Chief Financial Officer and Treasurer (Principal Financial Officer) pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.	
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## PART I. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

LINCOLN ELECTRIC HOLDINGS, INC.  
CONSOLIDATED STATEMENTS OF INCOME

(UNAUDITED)

(In thousands, except per share amounts)

	Three Months Ended March 31,	
	2014	2013
Net sales	\$685,062	\$718,573
Cost of goods sold	458,726	492,001
Gross profit	226,336	226,572
Selling, general & administrative expenses	145,915	136,891
Rationalization and asset impairment (gains) charges	(17	) 1,051
Operating income	80,438	88,630
Other income (expense):		
Interest income	914	1,026
Equity earnings in affiliates	1,561	1,259
Other income	1,083	714
Interest expense	(1,570	) (950
Total other income	1,988	2,049
Income before income taxes	82,426	90,679
Income taxes	26,002	23,836
Net income including non-controlling interests	56,424	66,843
Non-controlling interests in subsidiaries' (loss) earnings	(29	) 37
Net income	\$56,453	\$66,806
Basic earnings per share	\$0.70	\$0.81
Diluted earnings per share	\$0.69	\$0.80
Cash dividends declared per share	\$0.23	\$0.20

See notes to these consolidated financial statements.

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LINCOLN ELECTRIC HOLDINGS, INC.  
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME  
(UNAUDITED)  
(In thousands)

	Three Months Ended March 31,	
	2014	2013
Net income including non-controlling interests	\$56,424	\$66,843
Other comprehensive loss, net of tax:		
Unrealized (loss) gain on derivatives designated and qualifying as cash flow hedges, net of tax of \$94 and \$(113) in the three months ended March 31, 2014 and 2013	(421	) 602
Defined benefit pension plan activity, net of tax of \$1,838 and \$3,068 in the three months ended March 31, 2014 and 2013	2,544	5,105
Currency translation adjustment	(12,358	) (14,239 )
Other comprehensive loss:	(10,235	) (8,532 )
Comprehensive income	46,189	58,311
Comprehensive income attributable to non-controlling interests	652	150
Comprehensive income attributable to shareholders	\$45,537	\$58,161

See notes to these consolidated financial statements.

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LINCOLN ELECTRIC HOLDINGS, INC.  
 CONDENSED CONSOLIDATED BALANCE SHEETS  
 (In thousands)

	March 31, 2014 (UNAUDITED)	December 31, 2013 (NOTE 1)
<b>ASSETS</b>		
Current Assets		
Cash and cash equivalents	\$205,387	\$299,825
Accounts receivable (less allowance for doubtful accounts of \$8,365 in 2014; \$8,398 in 2013)	405,675	367,134
Inventories:		
Raw materials	103,913	112,478
Work-in-process	39,868	38,963
Finished goods	219,773	198,522
Total inventory	363,554	349,963
Other current assets	110,329	113,853
Total Current Assets	1,084,945	1,130,775
Property, Plant and Equipment		
Land	48,316	48,369
Buildings	375,041	373,373
Machinery and equipment	724,295	723,715
	1,147,652	1,145,457
Less accumulated depreciation	668,365	661,452
Property, Plant and Equipment, Net	479,287	484,005
Non-current assets	549,744	537,087
<b>TOTAL ASSETS</b>	<b>\$2,113,976</b>	<b>\$2,151,867</b>
<b>LIABILITIES AND EQUITY</b>		
Current Liabilities		
Amounts due banks	\$6,912	\$14,581
Trade accounts payable	199,739	212,799
Other current liabilities	224,870	228,822
Current portion of long-term debt	391	715
Total Current Liabilities	431,912	456,917
Long-Term Liabilities		
Long-term debt, less current portion	2,678	3,791
Accrued pensions	24,260	26,999
Other long-term liabilities	143,013	133,472
Total Long-Term Liabilities	169,951	164,262
Shareholders' Equity		
Common shares	9,858	9,858
Additional paid-in capital	244,824	240,519
Retained earnings	1,946,414	1,908,462
Accumulated other comprehensive loss	(162,857	) (151,941

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Treasury shares	(530,082	) (480,296	)
Total Shareholders' Equity	1,508,157	1,526,602	
Non-controlling interests	3,956	4,086	
Total Equity	1,512,113	1,530,688	
 TOTAL LIABILITIES AND EQUITY	 \$2,113,976	 \$2,151,867	

See notes to these consolidated financial statements.

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LINCOLN ELECTRIC HOLDINGS, INC.  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(UNAUDITED)  
(In thousands)

	Three Months Ended March 31,	
	2014	2013
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>		
Net income	\$56,453	\$66,806
Non-controlling interests in subsidiaries' (loss) earnings	(29)	) 37
Net income including non-controlling interests	56,424	66,843
Adjustments to reconcile Net income including non-controlling interests to Net cash provided (used) by operating activities:		
Rationalization and asset impairment (gains) charges	(35)	) 114
Depreciation and amortization	17,931	17,397
Equity earnings in affiliates, net	(796)	) (436)
Deferred income taxes	3,726	13,237
Stock-based compensation	2,293	2,468
Pension expense	2,800	7,615
Pension contributions and payments	(22,081)	) (55,321)
Foreign exchange loss (gain)	18,150	(1,162)
Other, net	(185)	) (198)
Changes in operating assets and liabilities, net of effects from acquisitions:		
Increase in accounts receivable	(43,885)	) (66,585)
Increase in inventories	(15,157)	) (16,334)
(Increase) decrease in other current assets	(1,420)	) 3,654
(Decrease) increase in trade accounts payable	(12,108)	) 8,268
Increase in other current liabilities	6,967	528
Net change in other long-term assets and liabilities	1,007	(236)
<b>NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES</b>	<b>13,631</b>	<b>(20,148)</b>
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>		
Capital expenditures	(14,506)	) (15,138)
Acquisition of businesses, net of cash acquired	(892)	) (549)
Proceeds from sale of property, plant and equipment	1,066	105
Other investing activities	573	—
<b>NET CASH USED BY INVESTING ACTIVITIES</b>	<b>(13,759)</b>	<b>) (15,582)</b>
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>		
Proceeds from short-term borrowings	1,018	390
Payments on short-term borrowings	(8,229)	) (1,455)
Amounts due banks, net	590	(280)
Payments on long-term borrowings	(1,435)	) (147)
Proceeds from exercise of stock options	2,956	9,658
Excess tax benefits from stock-based compensation	1,652	3,989
Purchase of shares for treasury	(51,021)	) (12,780)
Cash dividends paid to shareholders	(18,623)	) —
Transactions with non-controlling interests	(2,330)	) —
<b>NET CASH USED BY FINANCING ACTIVITIES</b>	<b>(75,422)</b>	<b>) (625)</b>



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Effect of exchange rate changes on Cash and cash equivalents	(18,888	) (1,654	)
DECREASE IN CASH AND CASH EQUIVALENTS	(94,438	) (38,009	)
Cash and cash equivalents at beginning of period	299,825	286,464	
CASH AND CASH EQUIVALENTS AT END OF PERIOD	\$205,387	\$248,455	

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LINCOLN ELECTRIC HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

Dollars in thousands, except per share amounts

NOTE 1 — BASIS OF PRESENTATION

As used in this report, the term “Company,” except as otherwise indicated by the context, means Lincoln Electric Holdings, Inc. and its wholly-owned and majority-owned subsidiaries for which it has a controlling interest. The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (“GAAP”) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, these unaudited consolidated financial statements do not include all of the information and notes required by GAAP for complete financial statements. However, in the opinion of management, these unaudited consolidated financial statements contain all the adjustments (consisting of normal recurring accruals) considered necessary to present fairly the financial position, results of operations and cash flows for the interim periods. Operating results for the three months ended March 31, 2014 are not necessarily indicative of the results to be expected for the year ending December 31, 2014.

The accompanying Consolidated Balance Sheet at December 31, 2013 has been derived from the audited financial statements at that date, but does not include all of the information and notes required by GAAP for complete financial statements. For further information, refer to the consolidated financial statements and notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2013.

Certain reclassifications have been made to the prior year financial statements to conform to current year classifications.

Venezuela — Highly Inflationary Economy

Venezuela is a highly inflationary economy under GAAP. As a result, the financial statements of the Company’s Venezuelan operation are reported under highly inflationary accounting rules as of January 1, 2010. Under highly inflationary accounting, the financial statements of the Company’s Venezuelan operation have been remeasured into the Company’s reporting currency and exchange gains and losses from the remeasurement of monetary assets and liabilities are reflected in current earnings. On February 8, 2013, the Venezuelan government announced the devaluation of its currency relative to the U.S. dollar. Effective February 13, 2013, the official rate moved from 4.3 to 6.3 bolivars to the U.S. dollar. During the three months ended March 31, 2013, the devaluation of the bolivar resulted in a foreign currency transaction loss of \$8,081 in Selling, general & administrative expenses and higher Cost of goods sold of \$1,579 due to the liquidation of inventory valued at the historical exchange rate.

In January 2014, the Venezuela government announced the formation of the National Center of Foreign Trade (“CENCOEX”) to replace the Commission for the Administration of Currency Exchange (“CADIVI”). Effective January 24, 2014, the exchange rate applicable to the settlement of certain transactions through CENCOEX, including payments of dividends and royalties, changed to utilize the Complementary System of Foreign Currency Administration (“SICAD”) auction-based exchange rate (the “SICAD I rate”) as opposed to the official rate. In February 2014, the government announced a new market based foreign exchange system, the SICAD II. The exchange rate established through SICAD II fluctuates daily and is significantly higher than both the official rate and the SICAD I rate.

While there remains considerable uncertainty as to the nature and volume of transactions that will flow through the various currency exchange mechanisms, the Company has determined that the SICAD I rate is the most appropriate exchange rate for the Company to utilize in remeasuring the Venezuelan operation's financial statements into U.S. dollars. This determination was made as a result of the Company's assertion as of March 31, 2014 that any future remittances for dividend payments could be transacted at the SICAD I rate. As of March 31, 2014, the SICAD I rate was 10.7 bolivars to the U.S. dollar, which resulted in a remeasurement loss on the bolivar-denominated monetary net asset position of \$17,665 which was recorded in Selling, general & administrative expenses in the three months ended March 31, 2014. Additionally, the Company expects higher Cost of goods sold of \$3,468 during the second quarter of 2014, due to the liquidation of inventory valued at the historical exchange rate. As previously discussed, the SICAD I rate is determined by periodic auctions and therefore the rate is likely to fluctuate in future periods which may result

in additional losses or gains on a remeasurement of the bolivar-denominated monetary net asset position. Future impacts to earnings of applying highly inflationary accounting for Venezuela on the Company's consolidated financial statements will be dependent upon the applied currency exchange mechanisms, the movements in the applicable exchange rates between the bolivar and the U.S. dollar and the amount of monetary assets and liabilities included in the Company's Venezuelan operation's balance sheet. The bolivar-denominated monetary net asset position was \$25,294 at March 31, 2014, including \$23,936 of cash and cash equivalents and \$38,633 at December 31, 2013, including \$50,642 of cash and cash equivalents.

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LINCOLN ELECTRIC HOLDINGS, INC.

NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS (Continued)

Dollars in thousands, except per share amounts

NOTE 2 — EARNINGS PER SHARE

The following table sets forth the computation of basic and diluted earnings per share:

	Three Months Ended March 31,	
	2014	2013
Numerator:		
Net income	\$56,453	\$66,806
Denominator:		
Basic weighted average shares outstanding	80,648	82,719
Effect of dilutive securities - Stock options and awards	968	1,067
Diluted weighted average shares outstanding	81,616	83,786
Basic earnings per share	\$0.70	\$0.81
Diluted earnings per share	\$0.69	