SYSCO CORP
Form 10-Q
May 10, 2007

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q

(Mark One)

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

For the quarterly period ended March 31, 2007

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 1-6544

SYSCO CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	74-1648137
(State or other jurisdiction of incorporation or organization)	(IRS employer identification number)

1390 Enclave Parkway
Houston, Texas 77077-2099
(Address of principal executive offices)
(Zip code)

Registrant s telephone number, including area code: (281) 584-1390

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 þ No o

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

Large Accelerated Filer þ Accelerated Filer o Non-accelerated Filer 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 þ

617,956,215 shares of common stock were outstanding as of April 28, 2007.

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PART I FINANCIAL INFORMATION

Item 1. *Financial Statements*

SYSCO CORPORATION and its Consolidated Subsidiaries
CONSOLIDATED BALANCE SHEETS
(In Thousands Except for Share Data)

	Mar. 31, 2007 (unaudited)	July 1, 2006	Apr. 1, 2006 (unaudited)
ASSETS			
Current assets			
Cash	$ 180,943	$ 201,897	$ 205,605
Accounts and notes receivable, less allowances of $60,105, $29,100 and $62,012	2,634,273	2,483,720	2,467,308
Inventories	1,693,084	1,608,233	1,601,250
Prepaid expenses	66,939	59,154	72,049
Prepaid income taxes		46,690	
Total current assets	4,575,239	4,399,694	4,346,212
Plant and equipment at cost, less depreciation	2,649,708	2,464,900	2,399,345
Other assets			
Goodwill	1,329,745	1,302,591	1,292,527
Intangibles, less amortization	89,977	95,651	97,733
Restricted cash	101,105	102,274	103,301
Prepaid pension cost	423,607	388,650	408,183
Other assets	257,940	238,265	236,787
Total other assets	2,202,374	2,127,431	2,138,531
Total assets	$ 9,427,321	$ 8,992,025	$ 8,884,088
LIABILITIES AND SHAREHOLDERS EQUITY			
Current liabilities			
Notes payable	$ 10,500	$ 29,300	$ 12,000
Accounts payable	1,982,126	1,891,357	1,839,477
Accrued expenses	810,216	745,781	736,798
Income taxes	119,919		47,647
Deferred taxes	357,629	453,700	346,980
Current maturities of long-term debt	104,882	106,265	208,570
Total current liabilities	3,385,272	3,226,403	3,191,472
Other liabilities			
Long-term debt	1,633,091	1,627,127	1,787,155
Deferred taxes	688,239	723,349	692,176
Other long-term liabilities	385,198	362,862	413,455

Total other liabilities	2,706,528	2,713,338	2,892,786
Commitments and contingencies			
Shareholders equity			
Preferred stock, par value $1 per share Authorized 1,500,000 shares, issued none			
Common stock, par value $1 per share Authorized 2,000,000,000 shares, issued 765,174,900 shares	765,175	765,175	765,175
Paid-in capital	618,087	525,684	498,322
Retained earnings	5,357,045	4,999,440	4,849,518
Other comprehensive income	67,441	84,618	19,870
	6,807,748	6,374,917	6,132,885
Less cost of treasury stock, 148,014,133, 146,279,320 and 146,967,829 shares	3,472,227	3,322,633	3,333,055
Total shareholders equity	3,335,521	3,052,284	2,799,830
Total liabilities and shareholders equity	$ 9,427,321	$ 8,992,025	$ 8,884,088

Note: The July 1, 2006 balance sheet has been derived from the audited financial statements at that date.

See Notes to Consolidated Financial Statements

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SYSCO CORPORATION and its Consolidated Subsidiaries
CONSOLIDATED RESULTS OF OPERATIONS (unaudited)
(In Thousands Except for Share and Per Share Data)

	39-Week Period Ended		13-Week Period Ended	
	Mar. 31, 2007	Apr. 1, 2006	Mar. 31, 2007	Apr. 1, 2006
Sales	$ 25,813,781	$ 24,119,361	$ 8,572,961	$ 8,137,816
Costs and expenses Cost of sales	20,856,982	19,517,648	6,938,867	6,602,102
Operating expenses	3,757,800	3,541,395	1,249,951	1,193,270
Interest expense	79,472	80,914	25,700	29,441
Other, net	(14,949)	(6,154)	(2,536)	(819)
Total costs and expenses	24,679,305	23,133,803	8,211,982	7,823,994
Earnings before income taxes and cumulative effect of accounting change	1,134,476	985,558	360,979	313,822
Income taxes	436,791	393,627	139,980	125,283
Earnings before cumulative effect of accounting change	697,685	591,931	220,999	188,539
Cumulative effect of accounting change		9,285		
Net earnings	$ 697,685	$ 601,216	$ 220,999	$ 188,539
Earnings before cumulative effect of accounting change:				
Basic earnings per share	$ 1.13	$ 0.95	$ 0.36	$ 0.30
Diluted earnings per share	1.11	0.94	0.35	0.30
Net earnings:				
Basic earnings per share	1.13	0.97	0.36	0.30
Diluted earnings per share	1.11	0.95	0.35	0.30
Average shares outstanding	618,988,223	621,995,157	617,678,739	618,973,143
Diluted shares outstanding	626,507,744	629,661,119	625,750,925	625,101,592
Dividends declared per common share	$ 0.55	$ 0.49	$ 0.19	$ 0.17

See Notes to Consolidated Financial Statements

SYSCO CORPORATION and its Consolidated Subsidiaries
CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (unaudited)
(In Thousands)

	39-Week Period Ended		13-Week Period Ended	
	Mar. 31, 2007	Apr. 1, 2006	Mar. 31, 2007	Apr. 1, 2006
Net earnings	$ 697,685	$ 601,216	$ 220,999	$ 188,539
Other comprehensive income, net of tax:				
Foreign currency translation adjustment	(17,497)	26,257	5,191	(2,217)
Change in fair value of forward-starting interest rate swap		7,064		
Amortization of cash flow hedge	320	226	107	107
Total other comprehensive income (loss)	(17,177)	33,547	5,298	(2,110)
Comprehensive income	$ 680,508	$ 634,763	$ 226,297	$ 186,429

See Notes to Consolidated Financial Statements

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SYSCO CORPORATION and its Consolidated Subsidiaries
CONSOLIDATED CASH FLOWS (unaudited)
(In Thousands)

	39-Week Period Ended	
	Mar. 31, 2007	Apr. 1, 2006
Operating activities:		
Net earnings	$ 697,685	$ 601,216
Adjustments to reconcile net earnings to cash provided by operating activities:		
Cumulative effect of accounting change		(9,285)
Share-based compensation expense	69,510	101,944
Depreciation and amortization	270,236	251,955
Deferred tax provision	405,228	365,548
Provision for losses on receivables	23,251	22,508
(Gain) loss on sale of assets	(5,791)	908
Additional investment in certain assets and liabilities, net of effect of businesses acquired:		
(Increase) in receivables	(170,145)	(158,778)
(Increase) in inventories	(86,722)	(118,535)
(Increase) in prepaid expenses	(7,933)	(11,333)
Increase in accounts payable	101,707	11,452
Increase in accrued expenses	54,167	15,387
(Decrease) in accrued income taxes	(352,399)	(449,976)
(Increase) in other assets	(26,976)	(18,040)
(Increase) decrease in prepaid pension cost and other long-term liabilities, net	(12,621)	39,724
Excess tax benefits from share-based compensation arrangements	(7,032)	(5,484)
Net cash provided by operating activities	952,165	639,211
Investing activities:		
Additions to plant and equipment	(457,174)	(363,909)
Proceeds from sales of plant and equipment	14,119	13,493
Acquisition of businesses, net of cash acquired	(48,534)	(109,423)
Increase in restricted cash	(1,331)	(1,570)
Net cash used for investing activities	(492,920)	(461,409)
Financing activities:		
Bank and commercial paper borrowings (repayments), net	(10,235)	282,460
Other debt borrowings	4,480	500,436
Other debt repayments	(7,418)	(209,625)
Debt issuance costs	(7)	(3,998)
Cash paid for termination of interest rate swap		(21,196)
Common stock reissued from treasury	184,950	104,782

Treasury stock purchases	(329,342)	(527,616)
Dividends paid	(328,029)	(293,535)
Excess tax benefits from share-based compensation arrangements	7,032	5,484
Net cash used for financing activities	(478,569)	(162,808)
Effect of exchange rates on cash	(1,630)	(1,067)
Net (decrease) increase in cash	(20,954)	13,927
Cash at beginning of period	201,897	191,678
Cash at end of period	$ 180,943	$ 205,605
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest	$ 86,733	$ 80,064
Income taxes	383,076	472,063

See Notes to Consolidated Financial Statements

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SYSCO CORPORATION and its Consolidated Subsidiaries
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Unaudited)

1. Basis of Presentation

The consolidated financial statements have been prepared by the company, without audit, with the exception of the July 1, 2006 consolidated balance sheet, which was taken from the audited financial statements included in the company s Fiscal 2006 Annual Report on Form 10-K. The financial statements include consolidated balance sheets, consolidated results of operations, consolidated statements of comprehensive income and consolidated cash flows. Certain amounts in the prior periods presented have been reclassified to conform to the fiscal 2007 presentation. In the opinion of management, all adjustments, which consist of normal recurring adjustments necessary to present fairly the financial position, results of operations, comprehensive income and cash flows for all periods presented, have been made.

These financial statements should be read in conjunction with the audited financial statements and notes thereto included in the company s Fiscal 2006 Annual Report on Form 10-K.

A review of the financial information herein has been made by Ernst & Young LLP, independent auditors, in accordance with established professional standards and procedures for such a review. A report from Ernst & Young LLP concerning their review is included as Exhibit 15.1.

2. Changes in Accounting

EITF 04-13 Adoption

In September 2005, the Emerging Issues Task Force (EITF) reached a consensus on Issue No. 04-13, Accounting for Purchases and Sales of Inventory With the Same Counterparty, which requires that two or more inventory transactions with the same counterparty (as defined) should be viewed as a single nonmonetary transaction if the transactions were entered into in contemplation of one another. Exchanges of inventory between entities in the same line of business should be accounted for at fair value or recorded at carrying amounts, depending on the classification of such inventory. This guidance was effective for the fourth quarter of fiscal 2006 for SYSCO. SYSCO has certain transactions where finished goods are purchased from a customer or sourced by that customer for warehousing and distribution and resold to the same customer. These transactions are evidenced by title transfer and are separately invoiced. Historically, the company has recorded such transactions in the Consolidated Results of Operations for purchases within Cost of Sales and sales within Sales. In fiscal 2007, the company recorded the net effect of such transactions in the Consolidated Results of Operations within Sales by reducing sales and cost of sales in the amount of $253,724,000 for the first 39 weeks and $76,718,000 for the third quarter. Prior to the adoption of EITF 04-13, the amounts included in the Consolidated Results of Operations on a gross basis within Cost of Sales for the 39 week and 13 week periods ended April 1, 2006 were $279,746,000 and $87,772,000, respectively. Such amounts were not restated when the new standard was adopted because only prospective treatment was allowed.

Pension Measurement Date Change

Beginning in fiscal 2006, SYSCO changed the measurement date for its pension and other postretirement benefit plans from fiscal year-end to May 31st, which represented a change in accounting. The one-month acceleration of the measurement date allows additional time for management to evaluate and report the actuarial pension measurements in the year-end

financial statements and disclosures within the accelerated filing deadlines of the Securities and Exchange Commission. The cumulative effect of this change in accounting was an increase to earnings in the first quarter of fiscal 2006 of $9,285,000, net of tax.

3. New Accounting Standards

FIN 48

In June 2006, the FASB issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes an Interpretation of FASB Statement No. 109 (FIN 48), which clarifies the accounting for uncertainty in income taxes recognized in accordance with FASB Statement No. 109 (SFAS 109). FIN 48 clarifies the application of SFAS 109 by defining criteria that an individual tax position must meet for any part of the benefit of that position to be recognized in the financial statements. Additionally, FIN 48 provides guidance on the measurement, derecognition, classification and disclosure of tax positions, along with accounting for the related interest and penalties. The provisions of FIN 48 are effective for fiscal years beginning after December 15, 2006, with the cumulative effect of the change in accounting principle recorded as an adjustment to opening retained earnings. SYSCO is currently evaluating the impact the adoption of FIN 48 will have on its consolidated financial statements.

SFAS 157

In September 2006, the FASB issued SFAS No. 157, Fair Value Measurements (SFAS 157). SFAS 157 defines fair value, establishes a framework for measuring fair value in accordance with generally accepted accounting principles, and expands disclosures about fair value measurements. The statement is effective for fiscal years beginning after November 15, 2007. The company is currently evaluating the impact of the provisions of SFAS 157.

SFAS 158

In September 2006, the FASB issued SFAS No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans an amendment of FASB Statements No. 87, 88, 106, and 132(R) (SFAS 158). SFAS 158 requires an employer to recognize a plan s funded status in its statement of financial position, measure a plan s assets and obligations as of the end of the employer s fiscal year and recognize the changes in a defined benefit postretirement plan s funded status in comprehensive income in the year in which the changes occur. SFAS 158 s requirement to recognize the funded status of a benefit plan and new disclosure requirements are effective as of the end of fiscal years ending after December 15, 2006. The requirement to measure plan assets and benefit obligations as of the date of the employer s fiscal year-end statement of financial position is effective for fiscal years ending after December 15, 2008. The company is currently evaluating the impact the adoption of SFAS 158 will have on its consolidated financial statements. The effect of adoption at June 30, 2007, SYSCO s adoption date, or any other future date, cannot be determined, since the impact is dependent upon on the measurements of each plan s assets and obligations at such date. However, if this standard had been applied at July 1, 2006, the result would have been an increase in current liabilities of approximately $10,000,000, an increase in other long-term liabilities of approximately $145,000,000, a decrease in prepaid pension cost of approximately $160,000,000, a decrease in deferred taxes of approximately $120,000,000 and a decrease in shareholders equity of approximately $195,000,000.

SFAS 159

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Liabilities (SFAS 159). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value that are not currently required to be measured at fair value. SFAS 159 also establishes presentation and disclosure requirements designed to facilitate comparisons between entities that choose different measurement attributes for similar types of assets and liabilities. SFAS 159 is effective as of the beginning of an entity s first fiscal year that begins after November 15, 2007. The company is currently evaluating the impact the adoption of SFAS 159 will have on its consolidated financial statements.

4. Restricted Cash

SYSCO is required by its insurers to collateralize a part of the self-insured portion of its workers compensation and liability claims. SYSCO has chosen to satisfy these collateral requirements by depositing funds in insurance trusts.

In addition, for certain acquisitions, SYSCO has placed funds into escrow to be disbursed to the sellers in the event that specified operating results are attained or contingencies are resolved. During the first 39 weeks of fiscal 2007, $4,000,000 was placed into escrow related to a new acquisition, and escrowed funds in the amount of $2,500,000 were released to sellers of acquired businesses. In addition, escrowed funds of $12,121,000 were released from escrow related to an acquisition for which the contingent consideration period expired without the additional consideration being earned.

A summary of restricted cash balances appears below:

	Mar. 31, 2007	July 1, 2006	Apr. 1, 2006
Funds deposited in insurance trusts	$ 92,105,000	$ 82,653,000	$ 81,980,000
Escrow funds related to acquisitions	9,000,000	19,621,000	21,321,000
Total	$ 101,105,000	$ 102,274,000	$ 103,301,000

5. Debt

In September 2006, the termination date on the revolving credit facility supporting the company s U.S. and Canadian commercial paper programs was extended from November 4, 2010 to November 4, 2011 in accordance with the terms of the agreement.

As of March 31, 2007, SYSCO had uncommitted bank lines of credit which provide for unsecured borrowings for working capital of up to $145,000,000, of which $10,500,000 was outstanding as of March 31, 2007.

As of March 31, 2007, SYSCO s outstanding commercial paper issuances were $408,133,000 and were classified as long-term debt since the company s commercial paper programs are supported by its long-term revolving credit facility in the amount of $750,000,000.

During the 39-week period ended March 31, 2007, the aggregate of commercial paper issuances and short-term bank borrowings ranged from approximately $356,804,000 to $703,072,000.

Included in current maturities of long-term debt at March 31, 2007 are the 7.25% senior notes due April 2007 totaling $100,000,000. In April 2007, SYSCO repaid these senior notes at maturity utilizing a combination of cash flow from operations and commercial paper issuances.

6. Employee Benefit Plans

The components of net benefit cost for the 39-week periods presented are as follows:

	Pension Benefits		Other Postretirement Plans	
	Mar. 31, 2007	Apr. 1, 2006	Mar. 31, 2007	Apr. 1, 2006
Service cost	$ 63,492,000	$ 75,021,000	$ 339,000	$ 384,000
Interest cost	68,484,000	62,703,000	399,000	354,000
Expected return on plan assets	(87,558,000)	(78,132,000)		
Amortization of prior service cost	4,264,000	3,699,000	151,000	151,000
Recognized net actuarial loss (gain)	7,266,000	34,653,000	(99,000)	(12,000)
Amortization of net transition obligation			114,000	114,000
Net periodic benefit cost	$ 55,948,000	$ 97,944,000	$ 904,000	$ 991,000

The components of net benefit cost for the 13-week periods presented are as follows:

	Pension Benefits		Other Postretirement Plans	
	Mar. 31, 2007	Apr. 1, 2006	Mar. 31, 2007	Apr. 1, 2006
Service cost	$ 21,164,000	$ 25,007,000	$ 113,000	$ 128,000
Interest cost	22,828,000	20,901,000	133,000	118,000
Expected return on plan assets	(29,186,000)	(26,044,000)		
Amortization of prior service cost	1,421,000	1,233,000	50,000	50,000
Recognized net actuarial loss (gain)	2,422,000	11,551,000	(33,000)	(4,000)
Amortization of net transition obligation			38,000	38,000
Net periodic benefit cost	$ 18,649,000	$ 32,648,000	$ 301,000	$ 330,000

SYSCO s contributions to its defined benefit plans were $68,168,000 and $71,538,000 during the 39-week periods ended March 31, 2007 and April 1, 2006, respectively.

Although contributions to its qualified pension plan (Retirement Plan) are not required to meet ERISA minimum funding requirements, the company anticipates it will make voluntary contributions of approximately $80,000,000 during fiscal 2007 of which $60,000,000 have been made in the first 39 weeks of fiscal 2007. The company s contributions to the Supplemental Executive Retirement Plan (SERP) and other post-retirement plans are made in the amounts needed to fund current year benefit payments. The estimated fiscal 2007 contributions to fund benefit payments for the SERP and other post-retirement plans are $10,300,000 and $300,000, respectively.

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7. Earnings Per Share

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

	39-Week Period Ended		13-Week Period Ended
	Mar. 31, 2007		